SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 278

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET AL.

No. 279

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

THE DENVER AND SALT LAKE WESTERN RAILROAD COMPANY, ET AL.

No. 280

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

CITY BANK FARMERS TRUST COMPANY, TRUSTEE, ET AL.

No. 281

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET AL.

No. 282

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, PETITIONERS,

vs.

GUY A. THOMPSON, TRUSTEE, ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

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INTERSTATE COMMERCE COMMISSION

Denver & Rio Grande Western Railroad Company Reorganization

SUBMISSION OF PLAN OF REORGANIZATION PURSUANT TO SECTION 77 OF THE BANKRUPTCY ACT, AS AMENDED

FINANCE DOCKET NO. 11002

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WASHINGTON, D. C.
APRIL, 1944

EXHIBIT A

INTERSTATE COMMERCE COMMISSION

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY
REORGANIZATION

Distribution of new securities per $1,000 principal amount of present bonds with accrued interest to January 1, 1943.

Outstanding Issue	Principal Amount Outstanding	Class of Present Security Designated in Court's Order of Classification	First Mortgage Bonds	Income Bonds	Preferred Stock	Common Stock
Denver & Rio Grande Consolidated 4's	$34,125,000	6	$318.92	$217.08	$321.60	$482.40
Denver & Rio Grande Consolidated 4½'s	6,382,000	6	329.03	223.97	331.80	497.70
Rio Grande Western First Trusts	15,190,000	7	970.20	349.80		
Rio Grande Western Consolidated's	15,080,000	8		266.00	970.90	93.10
Refunding and Improvement (Series A) 6's	2,000,000	10(a)	264.61	168.94	328.90	732.55
Refunding and Improvement (Series "B") 5's	12,000,000	10(b)	250.01	159.61	310.75	692.13
General 5's	29,808,009	11				146.10

Note: The treatment accorded the Reconstruction Finance Corporation and the Denver & Salt Lake bondholders and stockholders in case the consolidation provided for in the plan is or is not effected, is shown in Appendixes A and B on pages 182 and 183 hereof.

PLAN OF REORGANIZATION OF THE DENVER & RIO GRANDE WESTERN RAILROAD COMPANY, APPROVED BY THE COMMISSION IN ITS SUPPLEMENTAL ORDER OF JUNE 14, 1943, AND BY THE COURT, IN ITS ORDER OF OCTOBER 25, 1943.

Further investigation of the matters and things involved in this proceeding having been made upon petitions filed, and this Commission having, on the date hereof, made and filed a supplemental report containing its findings of fact and conclusions theron, and a full statement of the reasons for its conclusions, which report is hereby referred to and made a part hereof:

It is ordered, That the second supplemental report and order of July 13, 1942, approving a modified plan of reorganization of The Denver and Rio Grande Western Railroad Company, debtor, and The Denver and Salt Lake Western Railroad Company, secondary debtor, be, and it is hereby, further modified to read as follows, and as so further modified, is hereby approved:

Effective date.—A. The effective date of the plan shall be January 1, 1943.

The effective date of the plan shall determine the extent to which the claims of present creditors shall be capitalized in new securities, but the plan shall not affect creditors' claims until the new securities are actually issued by the reorganized company under the plan, and the carrying out of the plan shall not require any retroactive change in the operations of the debtor's trustees, or in their accounts, or in the reports made to this Commission or in any other reports or returns for the period prior to the date when such new securities are issued. Subject to the approval of the court, the reorganization committee may cause any issue of new securities to be dated as of a date other than the effective date (January 1, 1943), but only if the creditors who receive such issue of new securities shall receive the same treatment in respect of accruals of interest as if such issue of new securities had been dated January 1, 1943.

Reorganized company; consolidation.—B. The properties of the debtor, the secondary debtor, The Denver and Salt Lake Railway Company, hereinafter called the Salt Lake, The Rio Grande Junction Railway Company, hereinafter called the Junction, and the Goshen Valley Railroad Company, hereinafter called the Goshen Valley, shall, except as hereinafter otherwise provided, be merged or consolidated, to the extent legally possible, by transfer of the

subsidiary properties and the property held by the trustees, to the reorganized debtor or by transfer of all the properties to a new corporation organized for the purpose, hereinafter referred to as the new company, as may be determined by the reorganization committee. Consolidation of the Salt Lake with the debtor's properties shall be effective if, and only if, the holders of at least 90 percent in aggregate principal amount of Salt Lake income bonds voluntarily consent, within 90 days of the submission of the proposal to them to the modification of their rights, for which provision is hereinafter made. Unless such consents are obtained from the holders of the Salt Lake income bonds within the period stated, no actual consolidation of the Salt Lake and the Salt Lake Western with the debtor will be effective, and in that event only the properties of the debtor, the Junction, and the Goshen Valley shall be merged or consolidated in the manner indicated above; no provision will be made for the Salt Lake stock held by the public, and the trackage agreement will remain in effect. The merger or consolidation of the properties, including the Salt Lake, if the proposal is accepted by the holders of the required percent of bonds, shall be effected in a manner to be determined by the reorganization committee, subject to approval by this Commission and the court, and under a fair and equitable arrangement to protect the interests of the railroad employees affected, as required by law.

In the event that it appears to the judge that the consolidation of the Junction presents difficulties which may delay consummation of the plan in its application to the other interests, the judge may order consummation of the provisions of the plan other than those applicable to the distribution of securities to the Junction bondholders, and the Junction consolidation. Under these circumstances the Junction stock and the Junction lease should become assets of the reorganized company, subject to the liens of the mortgages of the reorganized company with provision for their release in the event of consolidation of the Junction with the reorganized company, and the Junction lease, in the discretion of the reorganization managers of the reorganized company and the judge, may be disaffirmed.

The new company shall be deemed to have come into possession of the properties as of the effective date of the plan.

New capitalization.—C. The capitalization of the new company, as of January 1, 1943, after consummation of the plan including the merger or consolidation of the Salt Lake, shall consist substantially of the following securities, excluding those to be pledged, the amounts stated being subject to reduction to the extent, if any, that matured interest proposed to be funded in the plan is paid, and

as equipment obligations or other liabilities are paid or reduced, and subject to variation as may be necessary, if so determined by the reorganization committee, to avoid the issue of scrip in denominations not expressible in even dollars or even hundredths of a share: Equipment-trust obligations, $5,758,000; new first-mortgage series A bonds, $38,573,680; new income-mortgage 4½-percent bonds, $29,750,184; bonds of the Denver & Salt Lake Railway Company, $11,234,000; a secured note or notes to the Chase National Bank, in the approximate amount of $2,158,458 (subject to a final determination of the amount of interest due on the present note, as of January 1, 1943); $32,531,220, par value, of new 5-percent preferred stock; and $35,167,585, par value, of new common stock.

In the event that the merger or consolidation of the Salt Lake is not effected, the capitalization of the reorganized debtor, as of January 1, 1943, excluding securities to be pledged, the amount stated being subject to reduction or variation, as provided above, shall consist substantially of $5,758,000 of equipment obligations, $33,373,680 of first-mortgage bonds, $21,049,579 of income bonds, a secured note or notes to the Chase National Bank in the approximate amount of $2,158,458, subject to the condition for such note stated above, the claim of the Finance Corporation, provided for in the manner hereinafter described, $32,120,120, par value, of 5-percent preferred stock, and $35,167,585, par value, of common stock.

Upon the consummation of the plan, including the consolidations, and the issue, distribution, and modification of securities as herein provided, the existing stocks of the debtor and its affiliated companies, together with all mortgage bonds issued and outstanding, including bonds pledged, and excluding all bonds of the Salt Lake, shall be surrendered to the reorganization committee and canceled, and all mortgages, other than the Salt Lake, shall be satisfied of record and canceled. In the event that consolidation of the Salt Lake is not effected, the stocks to be surrendered and canceled shall not include those of the secondary debtor and the Salt Lake.

Both the debtor and the secondary debtor shall be included within the plan.

The new company shall assume obligation in respect of all outstanding equipment obligations of the debtor and of the debtor's trustees. The interests of the holders of such claims are found not to be materially and adversely affected by the plan.

New first-mortgage bonds.—D. The new first mortgage shall constitute a first lien, subject only to the lien of equipment-trust obligations, on (1) all property owned by the debtor, the secondary debtor (in the event that consolidation with the Salt Lake is

effected, otherwise excluding the secondary debtor), or their trustees in bankruptcy as such, the Junction, and the Goshen Valley, at the time of effectuation of the plan, including securities, equipment, and the equity in such equipment as may be subject to equipment-trust obligations, but excluding the narrow-gage railway lines of the debtor, and equipment and property essential to the operation thereof, and excluding also the capital stock of the Utah Fuel Company; and (2) all property acquired by the new company after the date of the new first mortgage for use on or in connection with the mortgaged property subject only to such encumbrances or purchase-money liens as may exist or be created at the time of acquisition. So far as the reorganization committee, hereinafter provided for, may deem practicable, such lien shall be in the form of a direct mortgage, but it may take the form of the pledge or assignment of securities of a corporation or corporations owning property to which the lien is intended to extend. In the event of the consolidation of the properties of the Salt Lake as a part of the new system, the new first mortgage shall constitute a lien on such properties subject to the lien of the Salt Lake first-mortgage bonds and income bonds, so long as any of such bonds remain outstanding.

The first mortgage shall contain an appropriate provision in such terms as the reorganization committee shall determine, that the trustees under the mortgage may at any time release from the lien of the mortgage any of the mortgage property no longer required in the operation of the railroad, the proceeds from any sale or other disposition thereof to be equally and to the same extent held subject to the lien of the mortgage, as was the property so sold or disposed of. These provisions shall in no event operate to prevent the issue of equipment obligations with liens on equipment superior to the mortgage lien.

The first mortgage shall contain a covenant that the new company will at all times keep the mortgaged property supplied with such amount of motive power, rolling stock, and equipment (upon which the new first mortgage shall constitute a paramount lien subject only to such purchase-money liens as may be permitted by the terms thereof), and maintain the same in such condition as may be necessary for the efficient and economical operation of the mortgaged property.

The first-mortgage bonds may be issued in series, all equally secured as to principal and interest. Approximately $38,573,680 of series A bonds shall be issued in connection with the reorganization in partial settlement of claims, and additional series A bonds as may be necessary for the purpose of pledge, as provided in the plan. The series A bonds shall have a term of 50 years and shall

bear fixed interest at the rate of 3 percent per annum, and, in addition, fully cumulative prior contingent interest at the rate of 1 percent per annum, but subject to the right of the bondholders to postpone any interest payments, as hereinafter provided. Fixed interest shall be payable semiannually and prior contingent interest annually. Installments of interest on the new first-mortgage bonds becoming due before the plan is consummated shall be payable upon consummation of the plan.

The series A bonds shall be redeemable, in whole or in part, at a premium, initially not to exceed 5 percent, the rate thereof to be reduced during the life of the bonds according to a prescribed scale. Subject to such condition, the redemption provision shall be on such terms as the reorganization committee may determine.

Additional bonds, other than series A, shall be issuable under the mortgage without limit, or within such limit as may be specified in the mortgage, having such dates, maturities, coupon rates, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by this Commission. Such additional bonds shall be issuable on such bases, including the refunding of debt and the deposit of cash as shall be prescribed in the mortgage, provided that (1) bonds may be issued on the basis of additional property, including new equipment free from any other lien, and additions and betterments only to the extent of 75 percent, less prior lien debt, of the net amount of such additional property or additions and betterments, computed on the basis of cost, including prior lien debt, thereof or value thereof to the new company, whichever may be less; and (2), if consolidation with The Denver and Salt Lake Railway Company is effected in accordance with this plan, and when on any interest payment date for first-mortgage bonds the aggregate principal amount of new first-mortgage bonds outstanding, together with Denver and Salt Lake Railway Company first-mortgage bonds and income bonds, plus all other funded debt bearing fixed interest, shall exceed either 45 percent of total capitalization, as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest, other than bonds issued under the first mortgage, from 65 percent of the total capitalization at the time outstanding, the new company shall pay to the trustee of the new first mortgage, as a sinking fund, a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, prior contingent interest charges, the payment to the capital fund, contingent interest, and sinking-fund payments, as hereinafter prescribed; but, in the event such consolidation with The Denver and Salt Lake Railway Company is not

effected, the foregoing requirement of 45 percent for total fixed interest bearing debt shall be 40 percent. Such sinking fund shall be applied to the retirement of first-mortgage bonds by purchase in the open market or by call for tenders at not exceeding the redemption price (or in the case of bonds not redeemable, the principal amount and accrued interest), and, whenever the amount in the sinking fund exceeds $50,000 and first-mortgage bonds are not tendered or cannot otherwise be purchased at less than their redemption price, the funds then in the sinking fund shall be applied to the redemption of new first-mortgage bonds on the next succeeding interest payment date. All bonds so acquired shall be canceled, and no bonds may be issued to refund any such bonds. First-mortgage bonds and income mortgage bonds outstanding shall be deemed to include all bonds authenticated and delivered to the new company which shall not have been canceled or assured of retirement through the deposit of cash. Funded debt shall include an amount equal to the capitalized value at 5 percent per annum of fixed rents payable for leased roads, other than terminal properties, but shall not include *(a)* obligations, other than mortgage bonds or equipment trust obligations, maturing not more than 2 years after their date, or *(b)* obligations of longer maturity secured by pledge of bonds having a lien on property of the reorganized company except to the extent, if any, by which the principal amount of such obligations exceeds the principal amount of such bonds so pledged. Bonds which may be guaranteed by the new company as to interest or principal or both, other than bonds of a terminal company, shall be included in funded debt, but, in case of a joint or several guaranty with other corporations, only to the extent of the new company's basic proportion of the principal liability. There shall be included in determining total capitalization only *(a)* obligations constituting funded debt, *(b)* stock having par value, at such par value, and *(c)* stock without par value, at $100 a share, and, in case of other stock, at the capital value at which such stock is carried on the books of the company, not exceeding, however (except to the extent that earned surplus shall have been duly capitalized), the net amount received by the new company on the issue thereof; and (3) additional property, or additions and betterments acquired by the use of the capital fund hereinafter provided for shall not be eligible as a basis, in whole or in part, for the issue of bonds. Whenever any bonds shall be issued, or deposited cash withdrawn, on the basis of the acquisition of new equipment or to provide cash for such acquisition, an equipment sinking fund shall be established under which the new company will pay in cash to the trustee under the new first mort-

gage, on January 1 and July 1 of each year from available net income as hereinafter described, an installment of sinking fund equal to the quotient determined by dividing the principal amount of such bonds or the amount of cash so withdrawn by twice the number of years embraced in the original effective service life of such equipment, in no case to exceed fifteen, less the number of years of effective service life of the equipment which have elapsed since it was placed in service. Moneys held in such sinking fund shall be applied to the retirement of such bonds or of any new first-mortgage bonds as specified in the new first mortgage, by purchase at the lowest prices obtainable at public or private sale or upon calls for tenders or, to the extent not so applied, then if the amount of said moneys equals or exceeds $50,000, to the redemption of such bonds, in any case at not exceeding their redemption price. No bonds shall be issued on the basis of the acquisition of equipment under equipment-trust obligations or any obligations for the deferred or serial payment of purchase price, or on the basis of the retirement of any such obligations.

A sinking fund shall be provided for retirement of first-mortgage series A bonds to be issued in the reorganization, the annual payments to be equal to one-half of 1 percent of the largest principal amount of such bonds at any time previously authenticated and delivered, including bonds under pledge, such payments to be made if the available net income for the previous year is sufficient therefor after payment of all fixed charges, prior contingent interest, and payment into the capital fund, but before payment of contingent interest. Such payments shall not be cumulative. The sinking fund shall be applied to the retirement of first-mortgage series A bonds by purchase at not exceeding the current redemption price plus accrued interest, or by redemption. All first-mortgage bonds of series A so acquired shall be canceled, and no bonds of any kind issued to refund them.

The first mortgage shall contain a covenant substantially to the effect that the excess of the aggregate principal amount of all first-mortgage bonds under pledge at any one time, over the principal amount of all indebtedness so secured, shall not exceed 10 percent of the aggregate principal amount of all first-mortgage bonds then authenticated and uncanceled.

The new first mortgage shall provide, within conditions and limits to be therein prescribed, for the modification and alteration thereof, and of any or all supplements thereto, and of the rights and obligations of the new company thereunder and of the holders of the bonds at any time, by the concurrent action of the new company and of the holders of not less than two-thirds in aggregate

principal amount of the bonds then outstanding affected by such change or modification; provided that no such change or modification shall *(a)* alter or impair the obligation of the new company to pay the principal or interest of any bond at the time and place and at the rate and in the currency provided therein without the consent of the holder of such bonds, *(b)* permit the creation by the new company of any mortgage or lien in the nature of a mortgage ranking prior to or on a parity with the lien of the new first mortgage, except as in the new first mortgage otherwise expressly provided unless the creation of such mortgage or lien be consented to by the holders of all outstanding bonds, or *(c)* alter the specific provisions herein made for sinking funds nor the following provision with respect to the postponement of interest, without approval by this Commission. Notwithstanding the limitation in clause *(a)* in this paragraph, the obligation of the new company to pay interest on bonds issued in the reorganization for presently outstanding securities (and any other bonds as to which it may be so provided in the mortgage or any supplemental indenture) may be modified by the concurrent action of the new company and of the holders of not less than three-fourths in aggregate principal amount of such bonds then outstanding, so as to postpone the time of payment of any particular installments of interest, or any described number of installments of interest, until any fixed or determinable date or until the happening of any specified contingency, not in any case later than the date when the principal of such bonds shall be or become payable; but no postponement shall be made of any installment of interest in excess of a cumulative total of 10 semiannual installments excluding installments paid or as to which due provision for payment has been made; and before any such postponement becomes effective the holders of such bonds shall become, and until all postponed installments of interest be paid or due provision for payment thereof be made shall remain, entitled to elect the smallest number of directors necessary to constitute a majority of the full board.

New income-mortgage bonds.—E. The new income mortgage shall constitute a lien subject only to the lien of the first mortgage and any liens that may at the time be prior to the lien of the first mortgage, upon all property from time to time subject to the lien of the first mortgage.

The income mortgage shall contain an appropriate provision in such terms as the reorganization committee shall determine, that the trustees under the mortgage may at any time release from the lien of the mortgage any of the mortgaged property no longer required in the operation of the property and that the proceeds

from any sale or disposition thereof shall be equally and to the same extent held subject to the lien of the mortgage, as was the property so sold or disposed of.

The income-mortgage bonds may be issued in series, all equally secured as to principal and interest. Approximately $29,750,184 of series A income bonds shall be issued in the reorganization in partial settlement of claims, and additional bonds as may be necessary for the purpose of pledge, as provided in the plan. Additional bonds of other series shall be issuable without limit as to amount, or within such limit as may be specified in the mortgage, having such dates, maturities, rates of contingent interest, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by this Commission.

Such additional bonds shall be issuable on such bases, including the refunding of debt and the deposit of cash, as shall be prescribed therein, provided that (1) bonds may be issued on the basis of additional property, including new equipment free from any other lien, and additions and betterments only to the extent of 75 percent, less prior lien debt, of the net amount of such additional property or additions and betterments, computed on the basis of cost, including prior lien debt, thereof or value thereof to the new company, whichever may be less; and (2) additional property, except equipment free from any other lien, or additions and betterments acquired by the use of the capital fund, hereinafter provided for, shall not be eligible as a basis, in whole or in part, for the issue of income bonds. Whenever any income bonds shall be issued, or deposited cash withdrawn, on the basis of the acquisition of new equipment or to provide cash for such acquisition, an equipment sinking fund shall be established under which the new company will pay out of available net income, as hereinafter provided, to the trustee under the new income mortgage on January 1 and July 1 of each year an installment of sinking fund equal to the quotient determined by dividing the principal amount of such bonds or the amount of cash so withdrawn by twice the number of years embraced in the original effective service life of such equipment, in no case to exceed 15, less the number of years of service rendered by the equipment since first placed in service. Moneys held in such sinking fund shall be applied to the retirement of such bonds or of any new income-mortgage bonds as may be specified in the new income mortgage, by purchase at the lowest prices obtainable at public or private sale or upon calls for tenders or, to the extent not so applied, then if the amount of said moneys equals or exceeds $50,000, to the redemption of such bonds, in any case at not exceeding their redemption price. No bonds shall be

issued on the basis of the acquisition of equipment under equipment-trust obligations or any obligations for the deferred or serial payment of the purchase price, or on the basis of the retirement of such obligations.

The series A income-mortgage bonds to be issued in the reorganization shall have a term of 75 years and shall bear interest at the rate of 4½ percent per annum, payable annually. Such interest shall, within the limits of the accumulation hereinafter specified, become absolutely due as a debt on its due date each year in respect of the income period ending the next preceding December 31. Interest on the series A income-mortgage bonds shall, however, be mandatorily payable, except as otherwise provided by the last sentence in this paragraph, only out of available net income of the new company in respect of such income periods or, in the case of accumulations of interest, out of available net income in respect of such income periods or subsequent income periods; the board of directors of the new company may, however, in its discretion, cause the payment of interest on the bonds out of any funds whatever that may be lawfully available therefor. Interest on the outstanding income bonds, excluding bonds held in the sinking fund, shall be paid if covered by available net income, and, if not fully covered thereby, then to the extent so covered, in multiples of one-fourth of 1 percent; any available net income remaining undistributed shall, to the extent of the interest for such income period on the income bonds that accrued but was not paid, be held in the treasury of the new company and added to the available net income for the next succeeding income period. Interest on the series A income-mortgage bonds shall be cumulative to a maximum due at any one time of 18 percent of their principal amount, whether such amount represents interest for consecutive or nonconsecutive income periods. Accumulations of interest shall not bear interest. In case of accumulations of interest, the earliest due coupons or installments of interest shall be paid first. When the principal of any of the income bonds shall become payable, whether at maturity or upon redemption or by acceleration or in any other manner, or a permanent or confirmed appointment shall be made of any trustee or receiver for the new company or its property, all accumulated interest on such bond or bonds shall become immediately and absolutely payable regardless of earnings.

The series A income-mortgage bonds shall be redeemable, in whole or in part, on any interest payment date, on 30 days' notice by publication, at their principal amount plus interest at the rate of 4½ percent per annum accrued since the next preceding first day of April plus any unpaid accumulated interest. They shall be

entitled to the benefit of a sinking fund to be created by the payment on April 1 of each year of an amount equal to one-fourth of 1 percent of the aggregate principal amount of such bonds issued. Such payments shall be payable only out of available net income after payment, or setting aside for payment, of all accumulations of interest and of the full interest requirements at the rate of 4½ percent per annum for the applicable income period on the income bonds outstanding. Such payments for the sinking fund shall be cumulative to a maximum number at any one time of five installments, whether consecutive or non-consecutive installments. Moneys in the sinking fund shall be applied to the retirement of the series A bonds by purchase at the lowest prices obtainable at public or private sale or upon calls for tenders and, to the extent not so applied, then, if the amount of said moneys equals or exceeds $50,000, to the redemption of such bonds, in any case at not exceeding their redemption price. The bonds so purchased or redeemed shall be held alive in the sinking fund and shall continue to bear interest for the purposes of the sinking fund, and interest payable thereon, calculated at the rate paid for the applicable income period, including accumulations, on outstanding bonds, shall be added to the installments of sinking fund above provided for. No income-mortgage bonds shall be issued in lieu of the income bonds so purchased or redeemed for the sinking fund.

The new income mortgage shall provide, within conditions and limits to be therein prescribed, for the modification and alteration thereof, and of any or all supplements thereto, and of the rights and obligations of the new company thereunder and of the holders of the bonds at any time, by the concurrent action of the new company and of the holders of not less than two thirds in aggregate principal amount of the bonds then outstanding; and such modification or alteration may specifically include procedural provision for ascertaining available net income without the maintenance of separate books of account in the event that the new company shall be merged or consolidated or unified with a new company to result from the reorganization of The Western Pacific Railroad Company or with any other corporation; provided, however, that no such change or modification shall *(a)* alter or impair the obligation of the new company to pay the principal of or accumulated interest on any bond, or to pay interest on any bond out of available net income, as determined by the provisions hereof, or by any such alteration or modification of such provisions, at the time and place and at the rate and in the currency provided in such bond without the consent of the holder, of such bond, or *(b)* permit the creation by the new company of any mortgage or lien in the nature of a

mortgage ranking prior to or on a parity with the lien of the new income mortgage except as in the new income mortgage otherwise expressly provided, unless the creation of such mortgage or lien be consented to by the holders of all outstanding income bonds, or alter the provisions herein stated for sinking funds for the retirement of income bonds.

The income mortgage shall contain a covenant substantially to the effect that the excess of the aggregate principal amount of all income-mortgage bonds under pledge at any one time over the principal amount of all indebtedness so secured shall not exceed 10 percent of the aggregate principal amount of all income-mortgage bonds then authenticated and uncanceled.

Restrictions on additional mortgages, et cetera.—F. The new company shall not, without the consent of the holders of at least two-thirds in amount of the preferred and common stocks, voting as separate classes, (1) create or permit to be created any mortgage or other lien upon any of its properties, excepting the new first mortgage and new income mortgage, hereinbefore mentioned, and purchase-money liens, including equipment-trust liens, upon property hereafter acquired, given for not more than 75 percent of the purchase price of such property; (2) purchase or acquire, or contract to purchase or acquire, any property, or system of properties, at a cost to the new company of $5,000,000 or more, in cash or principal amount of par or book value of securities; (3) make any loans in an aggregate amount exceeding at any one time the aggregate amount of $200,000 to any subsidiary or parent or affiliated or other interest except by way of purchase of bonds of such borrower and pledge thereof under the new first mortgage subject to the conditions and restrictions to be provided therein; (4) merge or consolidate with any other corporation or dispose by sale or lease or otherwise of its assets as an entirety or substantially as an entirety; or (5) make any amendment to its charter or certificates of incorporation affecting the rights or interests of such stockholders.

In the event the new company shall be merged or consolidated or unified with a new company to result from the reorganization of The Western Pacific Railroad Company, or with any other corporation, then by vote or consent of two-thirds in par value of the preferred stock then outstanding procedural provision may be made for ascertaining available net income without the maintenance of separate books of account, and such provision shall be binding on all holders of stock of such class.

Determination and application of available net income.—G. The first mortgage and the income mortgage shall make appropriate

provision for the determination and application of available net income and a capital fund as follows:

The available net income of the new company shall be determined for each calendar year ending December 31. The available net income for each such income period shall equal the remainder left after deducting from the income of the new company arising from the properties subject to the lien of the new income mortgage and from the properties or systems acquired by the new company under the plan which is available for fixed charges for such income period (determined in accordance with the accounting rules of this Commission at the time in force or other analogous Federal authority having jurisdiction at the time, or, to the extent not covered by such accounting rules, in accordance with sound accounting practice) such part of the following amounts as arise in the operation of, or are incident to, the aforesaid properties; namely:

(a) All fixed charges, determined in accordance with such accounting rules or practice of the new company accrued during such income period, including fixed interest payments on the Salt Lake first-mortgage bonds and income bonds in the event consolidation with the Salt Lake is effected under the plan; provided, however, that, if in any income period the new company shall fail to earn such fixed charges, the amount of such deficit may, in the discretion of the board of directors of the new company (and shall in the event that funds shall have been borrowed because of such deficit to pay such fixed charges), be paid out of income for the next ensuing period or periods before determining available net income, and any income so deducted before determining available net income shall be first used to retire any indebtedness that may have been incurred for the purpose of paying such fixed charges;

(b) All other charges properly deductible from such income in determining income after fixed charges under such accounting rules or practice, but excluding contingent interest and sinking fund requirements, hereinafter provided for;

(c) The sum, subject to the proviso set out below, of 2½ percent of total railway operating revenues (determined in accordance with such accounting rules or practice) of the new company for such income period, subject to a maximum limit of $750,000 for each 12-month period, which sum shall constitute the capital fund and be disposed of as hereinafter set forth. Any amount by which such income in any income period shall be inadequate to provide for the capital fund, i. e., shall fall below 2½ percent of total railway operating revenues, subject to the aforesaid maximum, shall accumulate and be carried forward, as an additional requirement of the capital fund, into the next succeeding income period, but not

beyond; provided that payments into the fund in any calendar year shall not exceed the sum necessary to bring the total in the fund to $1,500,000 after all withdrawals from the fund during the same year as hereinafter provided for; and

(d) All payments to sinking funds which may have been established, as provided above, for the retirement of first-mortgage bonds issued for the acquisition of equipment free of other lien.

The available net income for each income period shall be applied to the following purposes and in the following order:

(1) All available net income shall, to the extent required, and subject to the provision hereinbefore made for payment in even multiples of one-fourth of 1 percent and postponement of fractional surplus, be applied to the payment, on April 1 in each year, of prior contingent interest at the rate of 1 percent per annum, pro rata on the first-mortgage bonds, series A, of the new company then outstanding and on the modified Salt Lake income bonds outstanding, in the event of consolidation with the Salt Lake; otherwise on the first-mortgage bonds of the new company only.

(2) Any then remaining available net income shall be applied to the payments to sinking funds, if any, which may have been established for the retirement of income bonds issued for the acquisition of equipment free of other liens.

(3) Any then remaining available net income shall be applied on April 1 of each year to the general sinking fund for retirement of the first-mortgage bonds, series A, as specified under section E of this order.

(4) Any then remaining available net income shall, to the extent required and subject to the provision hereinbefore made for payment in even multiples of one-fourth of 1 percent and postponement of fractional surplus, be applied in the payment on April 1 of each year to interest on the then outstanding income-mortgage bonds of the new company, excluding bonds then held in the sinking fund under the new income mortgage, but including bonds under pledge, accruing during the income period ending on the next preceding December 31, and to the payment of any unpaid accumulated interest on said bonds.

(5) Any then remaining available net income shall be applied, until all the income bonds of the new company shall have been retired, on April 1 in each year to a sinking fund for such bonds in an amount up to, but not exceeding, in respect of any income period, one-fourth of 1 percent of the total principal amount of income bonds issued, plus an amount equal to the interest on income bonds theretofore purchased or redeemed for the sinking fund, calculated at the rate paid, pursuant to the foregoing clause

(4), in respect of such income period, including accumulations, upon outstanding income bonds. Any amount by which the available net income remaining for such purpose is inadequate to pay the full amount of such installment of sinking fund shall be cumulated within the limits hereinabove stated and added to the installments payable in the next ensuing income period or periods.

(6) Any then remaining available net income shall be applied to payment to the sinking fund to be created and paid to the trustee under the first mortgage in the event the principal amount of first-mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either *(a)* 45 percent of the total capitalization of the new company, determined as elsewhere provided in the plan on the basis of consolidation with the Salt Lake, or 40 percent without such consolidation, or *(b)* the result obtained by deducting the principal amount of funded debt, other than first-mortgage bonds, bearing contingent interest, from 65 percent of the total capitalization at the time outstanding.

(7) Any then remaining available net income shall be applied, as may be declared by the board of directors, to the payment of dividends in the order of their priority or to other proper corporate purposes.

The available net income for any period after December 31, 1942, until the new company comes into ownership and possession of the properties of the companies embraced in the plan, or of their trustees in bankruptcy, shall be computed as if the new company had come into such ownership and possession on January 1, 1943, and had issued, as of that date, the new securities issuable under the plan and had assumed obligation with respect to interest on the Salt Lake bonds.

Capital fund.—H. The above provisions for the deduction of the capital fund from the income of the new company available for fixed charges are subject to the following proviso: If the new company shall establish and maintain, in such manner as may be permitted or required by law or lawful regulation, an operating expense account for depreciation of its roadway and structures, then *(a)* the capital fund shall be paid from the reserve for depreciation on roadway and structures so credited in respect of the applicable income period to the extent that the amount so credited to said depreciation reserve shall be adequate therefor; *(b)* to that extent the foregoing provisions for the deduction of the capital fund shall cease to be operative; and *(c)* the new company shall not be entitled to withdraw any moneys from the capital fund until it shall have expended in the current calendar year for additions and betterments properly chargeable to capital account under

said accounting rules or practice more than the amount by which its charge for depreciation of roadway and structures in such year, less cash expenditures incurred in the making of retirements properly charged to the depreciation reserve so credited, exceeds the total paid into the capital fund in such year and then only to the extent of such excess.

The capital fund shall be accumulated through the deposit of funds on April 1 of each year and shall, subject to the proviso in the next preceding paragraph, be withdrawable by the new company to reimburse it for, or to provide for:

(a) All of the cost, payable in cash, of additions and betterments to the mortgaged property, including equipment, which are properly chargeable to capital account under said accounting rules or practice, and not previously certified or thereafter to be certified to the trustee under the new first mortgage as the basis, in whole or in part, for the issue of additional new bonds, or the release of mortgaged property or the withdrawal of cash held by such trustee, and further provided that no expenditures so used as a basis for the withdrawal of any moneys from the capital fund shall be made the basis for the issue by the new company of any form of indebtedness or stock ranking prior to or on a parity with the new preferred stock;

(b) All of the amount by which the unfundable purchase price, as hereinafter defined, for new equipment exceeds equipment depreciation surplus, as hereinafter defined. In the case of equipment acquired under equipment-trust obligations, the unfundable purchase price shall equal the initial or down payment for such equipment. In the case of equipment acquired and paid for by the withdrawal of deposited cash under either of the new mortgages, the unfundable purchase price shall equal that part of the purchase price not so withdrawable. Equipment depreciation surplus shall equal the remainder determined by deducting (1) the total installments of principal of equipment-trust obligations or other obligations for the deferred or serial payment of the purchase price for equipment, and installments of equipment-sinking funds paid out of equipment depreciation, as hereinabove provided in the next preceding income period, from (2) the total charges to operating expenses in such income period for depreciation of equipment. Such withdrawals from the capital fund shall be permitted only on the basis of such payments for equipment made or to be made in the calendar year in which the payment of such moneys into the capital fund is due; and

(c) For the purpose of paying fixed interest on the bonds outstanding under the new first mortgage in a year or years in which

the net earnings of the new company available for interest on said bonds shall be inadequate for the payment of such interest, and only to the extent of such inadequacy.

New stock issues.—I. The preferred stock of the new company shall be authorized in the total amount of 500,000 shares, of the par value of $100 each, of which approximately 325,312 shares shall be issued in the reorganization, excluding shares which shall be issued for pledging purposes. Such stock shall be entitled to receive dividends out of available net income as hereinabove provided, or out of earned surplus from prior income periods, when and as declared by the board of directors of the new company, at the rate of 5 percent per annum in respect of each calendar year beginning January 1, 1943, before any dividends shall be paid or declared or set apart for payment on the common stock. Such dividends shall be cumulative to the extent earned in respect of any income period but not paid, but such dividends shall otherwise be noncumulative. In any liquidation or winding up or distribution of the assets of the new company, whether voluntary or involuntary, the new preferred stock shall be entitled to receive, out of the assets of the new company, its par value plus any accrued and unpaid cumulative dividends thereon, before any distribution shall be made to any common stock, but shall not be entitled to any further participation in any such assets. The new preferred stock shall be redeemable in whole or in part at any time at its par value plus accumulated and unpaid dividends and proportionate dividend for the current year. The new preferred stock shall be convertible at the option of the holder at any time, except that stock which is called for redemption shall be convertible not later than 15 days prior to the date as of which such call shall be made, into new common stock at the rate of 1 share of common stock for each share of preferred stock.

The common stock of the new company shall be authorized in the total amount of 1,000,000 shares, having a par value of $100 a share, and approximately 351,676 shares shall be issued in reorganization, excluding shares to be pledged, and approximately 325,312 shares shall be reserved for conversion of the preferred stock.

The preferred stock and common stock shall have equal voting rights, each share being entitled to one vote in the election of directors and in all matters of proprietary interest; provided, however, that the holders of the preferred stock, voting as a class, shall always have the right to elect not less than one-third, and in no event less than two, of the members of the board of directors. Cumulative voting shall be permitted.

Treatment of claims and distribution of new bonds, stock, et cetera.—J. In the event that consolidation of the Salt Lake properties is to be effected as provided herein; the Reconstruction Finance Corporation shall receive, in payment of the debtor's and secondary debtor's notes to it, with accrued interest to December 31, 1942, $5,200,000 of new first-mortgage bonds and $8,700,605 of new income bonds plus the amount of the rental or other use and occupation claim of the Salt Lake Western trustee against the principal debtor's trustees which may be allowed by the court. Upon receipt of such new securities, the Reconstruction Finance Corporation shall deliver to the reorganization committee all the securities now held under pledge.

Nothing contained herein shall be construed as limiting in any manner affecting the right of the Finance Corporation to apply, in its discretion, the income on and the proceeds of the collateral held by it to or toward the payment of the principal or interest, or both, to or upon its claim against the debtor prior to the consummation of the reorganization.

In the event consolidation of the Salt Lake is not to be effected as herein provided, the claim of the Reconstruction Finance Corporation shall be provided for as follows: For the $1,445,000 of Denver & Rio Grande Railroad Company consolidated-mortgage 4-percent bonds, $10,000 of Rio Grande Western Railway Company first trust 4-percent bonds, $1,395,000 of the Rio Grande Western Railway Company consolidated-mortgage 4-percent bonds, and $4,385,000 of the debtor's refunding and improvement mortgage 5-percent bonds, pledged as part security for the loans, the Reconstruction Finance Corporation shall be entitled to receive $1,566,846 of new first-mortgage bonds, $1,388,150 of new income bonds, $3,181,757 of new preferred stock, and $3,861,910 of new common stock. These new securities, together with the $1,266,600 of Denver & Salt Lake income bonds, 500 shares of Goshen Valley stock, $1,777,000 of Rio Grande Southern first-mortgage bonds, 73,710 shares of Denver-Colorado Springs-Pueblo Motorway stock, 2,262 shares of Rio Grande Motorway stock, 45,889 shares of Denver & Salt Lake stock, and 36,310 shares of Salt Lake Western stock, now held in pledge, shall be deposited under an escrow agreement with a bank or trust company designated by the court, and escrow receipts therefor shall be issued to the Reconstruction Finance Corporation. The agreement shall be for a term of 6 years, and shall provide that the escrow agent (1) shall, at the request of the Reconstruction Finance Corporation, sell all or any part of the deposited securities at such price or prices as may be stated in the request, subject in the case of the sale of the stock of

the Denver & Salt Lake, and of the Denver & Salt Lake Western, to anyone other than the new company, to the approval of this Commission both as to the sale and as to the price to be paid, and (2) shall impound any or all receipts from the deposited securities, whether from sale, dividends, or interest, and make payments of same promptly to the Reconstruction Finance Corporation which shall agree to credit such receipts first against the interest accrued on the claim of $12,900,605 from January 1, 1943, to date at the rate of 4 percent per annum, and further agree to apply any funds received in excess of such interest requirement to reduction of the principal of the claim; *provided, however,* (1) that the new company shall have the right to purchase at any time all of the stock of the Salt Lake, or of the Salt Lake Western, which the Reconstruction Finance Corporation shall have requested the escrow agent to sell, at the price or prices stated in such request; (2) that if, prior to the expiration of the escrow agreement, the total sum paid through the foregoing means to the Reconstruction Finance Corporation shall equal the total amount due on the claim with accrued interest, the securities remaining in the hands of the escrow agent, together with any cash on hand after settlement of the said debt, shall forthwith be turned over to the new company; and (3) that, if at the expiration of the escrow agreement, the claim of the Reconstruction Finance Corporation shall not have been discharged in full, all the securities remaining on deposit, together with any cash balance, shall be turned over to the Reconstruction Finance Corporation in final settlement of its claim, subject, however, to the right of the new company, prior to such transfer, to acquire all of such securities by payment of the balance then due on the Reconstruction Finance Corporation claim, including interest.

It shall be provided that the Reconstruction Finance Corporation shall be bound by the terms of any sale or sales to which it has consented and which have been approved by this Commission. During the life of the escrow agreement, the Reconstruction Finance Corporation shall have the right to receive notice of all meetings of the holders of stocks under deposit and to direct the escrow agent as to the manner in which stocks represented by the escrow receipts shall be voted at such meetings. In the absence of such directions, the deposited stocks shall be voted in such manner as the escrow agent may determine. The reasonable compensation and expenses of the escrow agent shall be paid by the new company.

The money value of any award for the rental or other use and occupation claim of the Salt Lake Western trustee against the principal debtor's trustees, as allowed by the court, shall be paid

over to the Reconstruction Finance Corporation and the amount of the claim, or of the face amount of any note evidencing the indebtedness, correspondingly reduced without otherwise affecting the foregoing provisions with respect to the discharge of the claim where consolidation is not to be carried out.

K. The holders of bonds of the classes shown below shall receive for each $1,000 bond and all unpaid interest thereon, as of the effective date of the plan, substantially the following amounts of new securities:

Rio Grande Western Railway Company first-trust bonds, $970.20 of new first-mortgage bonds and $349.80 of new income bonds; Rio Grande Western Railway Company consolidated-mortgage bonds, $266.00 of new income bonds, $970.90, par value, of new preferred stock, and $93.10, par value, of new common stock; Rio Grande Junction Railway Company first-mortgage bonds, $1,061.96 of new first-mortgage bonds and $317.21 of new income bonds; Denver & Rio Grande Railroad Company consolidated mortgage 4-percent bonds, $318.92 of new first-mortgage bonds, $217.08 of new income bonds, $321.60, par value, of new preferred stock, and $482.40, par value, of new common stock; Denver & Rio Grande Railroad Company consolidated-mortgage 4½-percent bonds, $329.03 of new first-mortgage bonds, $223.97 of new income bonds, $331.80, par value, of new preferred stock, and $497.70, par value, of new common stock; the debtor's refunding and improvement mortgage 5-percent bonds, $250.01 of new first-mortgage bonds, $159.61 of new income bonds, $310.75, par value, of new preferred stock, and $692.13, par value, of new common stock; the debtor's refunding and improvement mortgage 6-percent bonds, $264.61 of new first-mortgage bonds, $168.94 of new income bonds, $328.90, par value, of new preferred stock, and $732.55, par value, of new common stock; and the debtor's general mortgage bonds, $146.10, par value, of new common stock.

The interests or equities of (1) all general unsecured creditors of the debtor whose claims are not entitled to priority over the mortgages of the debtor, (2) holders of preferred stock of the debtor, and (3) holders of common stock of the debtor have no value and nothing shall be distributable to them.

Scrip shall be issued for sums less than $100 in the case of bonds, and for fractional shares of stock.

The trustee under the Rio Grande Western Railway Company consolidated mortgage shall be permitted to obtain the release of the equities in the stock of the Utah Fuel Company and distribute the stock among the holders of the aforesaid bonds in any manner

agreeable to them, or to enforce its rights as pledgee of the stock of the Utah Fuel Company, the proceeds recovered to be distributed to the holders of the bonds.

The new company shall pay, in cash, all interest coupons on the bonds or equipment obligations of the debtor or its subsidiaries other than the Denver and Salt Lake Railway Company which had been declared payable but had not been paid prior to November 1, 1935, if and when such coupons are presented by the holders thereof.

There shall be set aside, for securities issued in the reorganization of 1924 which have not been claimed, new securities under the plan herein approved to the same extent as for like outstanding securities of the debtor, or those claims shall be settled in cash as may be determined by the court.

The secured note held by the Chase National Bank shall be canceled, and a new note or new notes issued in face amount equal to that of the present note, plus interest accrued to January 1, 1943, in the amount of $2,158,458, or such other amount as may be allowed by the court, such notes to mature in 10 years, and to bear interest at the rate of 4 percent per annum, payable semiannually on October 1 and April 1 of each year, but such interest shall be contingent on, and payment thereof shall be limited to, the total of the interest and dividends paid by the new company on the collateral securing such notes. The interest shall be cumulative to the maximum amount at any one time of 16 percent (whether for consecutive or nonconsecutive income periods). Any interest and/or dividends paid upon the pledged collateral in excess of interest requirements on such notes (including accumulations of interest) shall be applied to the payment of the principal amount of such notes. Such notes may be redeemed in whole or in part at any time on 30 days' notice at their principal amount plus full interest at the rate of 4 percent per annum accrued since the last preceding April 1, and all unpaid accumulated interest. Upon the payment or other retirement of all such notes, the collateral securing them shall be returned to the new company, and the new company shall, in the case of certificates of stock, cancel and retire the same, and in the case of bonds deliver the same forthwith to the trustee under the indenture securing the same for cancelation and retirement; no bonds shall be issued in lieu of any bonds so canceled and retired. The new securities issuable as collateral shall consist of not exceeding $1,524,076 of new first-mortgage bonds, $972,998 of new income bonds, $1,894,332 of new preferred stock, and 42,192 shares of new common stock.

The proposal to be submitted to the holders of the Salt Lake

income bonds; constituting the terms upon which consolidation of the Salt Lake shall be carried out, shall be that (1) the maturity of such bonds shall be extended to that of the first-mortgage series-A bonds to be issued by the new company, and (2) that the interest terms of the present bonds be modified to provide for fixed interest at the rate of 3 percent per annum and fully cumulative prior contingent interest at the rate of 1 percent per annum, and both payable when fixed and prior contingent interest, respectively, are payable on the new first-mortgage bonds, subject to the right of the new company, as in the case of the new first mortgage, described above, to postpone the payment of installments of interest by the concurrent action of the new company and the holders of not less than three-fourths of the total amount of income bonds outstanding. The proposal shall be presented to the bondholders in the form determined by the reorganization committee, and the committee shall report the results to the court. If the holders of 90 percent or more of the income bonds outstanding shall accept the proposal within 90 days of its submission to them, the consolidation of the Salt Lake properties with the debtor's properties shall be carried out, as herein provided. The reorganization committee shall be authorized to call for payment any Salt Lake income-mortgage bonds the holders of which shall not have assented to the proposed modification of terms, or to arrange for the refunding or purchase of such bonds, at the convenience of the new company.

In the event of consolidation with the Salt Lake on the basis herein provided, the new company shall assume all the obligations under the two Salt Lake mortgages, as stated therein in case of a merger into any other company, including the assumption of the obligation with respect to the payment of the principal and interest of all bonds now outstanding, except as the terms of the Salt Lake income bonds shall be modified, as provided above. No additional bonds shall be issued under either of the Salt Lake mortgages. The new company shall also assume the present tunnel contract, and the trackage agreement shall be canceled.

The holders of stock of the Salt Lake outstanding in the hands of the public shall, in the event the merger or consolidation of that railroad is effected under the plan, be entitled to receive therefor the preferred stock of the new company on the basis of one share of such stock for each share of Salt Lake stock.

In view of possible changes in the amounts of the obligations herein shown as outstanding, the reorganization committee shall be authorized, in order to give effect to such changes, to make such adjustments in the claims provided for in the plan, and such

changes in allotment of securities, consistent with the provisions of the plan, as may be approved by the court.

New financing.—L. Any cash that may, in the judgment of the reorganization committee, be needed in reorganization, but in no event to exceed $2,000,000, shall be advanced by the Reconstruction Finance Corporation or obtained through private channels and evidenced by collateral note of the new company for a term of 12 years, secured by pledge of new first-mortgage bonds in an amount equal to 125 percent of the loan, or such other amount of bonds as may be required by the lender and approved by this Commission. As an alternative to such a loan, not exceeding $2,500,000 of new first-mortgage bonds may be issued for sale to provide the new money required, under terms and conditions to be determined by the reorganization committee and approved by the court and this Commission.

Voting trust for new stock.—M. All the preferred stock and all the common stock, issued by the new company in reorganization, excepting shares issued to qualify directors, shall be deposited under an escrow agreement with a bank or trust company designated by the court, and escrow receipts issued to persons entitled to receive such stock under the plan. The escrow agreement shall be for a term of 10 years from the date of creation of the trust, such term to be considered as beginning not later than 6 months after confirmation of the plan, and shall provide that the reorganization committee, as voting trustees, may, subject to the approval of the Commission, and with the consent of the holders of escrow receipts representing not less than two-thirds of the shares of preferred stock on deposit, sell all or any part of such preferred stock at such price or prices as they may deem advantageous to the interest of the new company and its stockholders; likewise the voting trustees may sell all or any part of the deposited common stock, with the consent of the holders of escrow receipts representing not less than two-thirds of the shares of such common stock.

It shall be provided that all holders of escrow receipts shall be bound by the terms of any sale or sales which shall have been approved by this Commission and consented to as aforesaid, and the net proceeds of any sale or sales, together with any unsold stock, shall be distributed pro rata among the holders of the escrow receipts for preferred stock and common stock, respectively, according to the class of stock sold. During the life of the escrow agreement, the holders of escrow receipts shall have the right to receive notice of all meetings of stockholders and to direct the voting trustees as to the manner in which the stock represented by the escrow receipts shall be voted at such meetings. In the absence

of such directions, the deposited stock shall be voted in such manner as the voting trustees may determine. The reasonable compensation and expenses of the voting trustees, including counsel fees, shall be paid by the new company.

Directors.—N. The number of directors of the new company and the manner of their election shall be determined by the reorganization committee and provided in the new charter or an amendment of the debtor's present charter.

Leases, agreements, et cetera.—O. In the event consolidation of the various companies, including the Salt Lake, shall be effected, as herein provided, the new company may take any action with respect to the lease or agreement with the Northwestern Terminal Railroad Company as may be lawful under the terms thereof. As to all other agreements and executory contracts, including the existing lease agreement of the Salt Lake with the Moffat Tunnel Improvement District, the new company shall be deemed to have assumed the obligations with respect to such agreements and contracts which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding and which shall not have been disaffirmed by the trustees of the respective estates with the approval of the court prior to confirmation of the plan, and the new company shall also assume any executory contracts made by the trustees, with the approval of the court, which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding.

In the event consolidation of the Denver & Salt Lake is not effected, the foregoing provisions with respect to the lease agreements with the Northwestern Terminal Railroad Company and the Moffat Tunnel Improvement District shall not apply, and the assumption of obligation by the new company with respect to agreements and contracts shall be confined to those entered into with the debtor and its affiliated companies but not those entered into with the Denver & Salt Lake but not with the debtor.

Claims against the debtor and its subsidiaries entitled to priority over their respective mortgages, claims for taxes levied, assessed, or accrued against the debtors, their subsidiaries, or trustees, current liabilities and obligations incurred by the trustees during the reorganization proceedings, to the extent unpaid at the date of confirmation of the plan, and claims arising from the disaffirmance of executory leases or contracts of the trustees pursuant to orders of the court, in respect of which claims are filed or evidenced in accordance with orders of the court, shall be assumed by the new company, and paid in the usual course of business with the same

relative priority as they now have with respect to other obligations of the debtor or its subsidiaries.

Expenses of reorganization.—P. The expenses of reorganization, as allowed by the court, subject to the provisions of section 77, shall be paid in cash.

Reorganization committee.—Q. A reorganization committee shall be created which shall carry out the plan under the supervision and control of the court. It shall consist of five members, two to be designated by the insurance group committee as representatives of the Rio Grande Western first-mortgage bonds, the Junction first-mortgage bonds, the Denver & Rio Grande consolidated-mortgage bonds, and the Rio Grande Western consolidated-mortgage bonds, one to be designated jointly by the trustee under the debtor's refunding and improvement mortgage and the trustee under the debtor's general mortgage, one by the Reconstruction Finance Corporation as its representative, and one by the judge of the United States District Court for the District of Colorado. Should any of the parties named fail to designate its representative or representatives, as the case may be, within such time as the court shall consider reasonable, the court shall appoint such representative or representatives. The reorganization committee may fill any vacancies created by death, resignation, or otherwise, preserving the representation of the several interests as before. The members of the committee as such, shall agree to serve without compensation, but its expenses shall be paid by the new company, subject to the provisions of section 77 and the approval of the court, as part of the cost of the effectuation of the plan. In their capacity as voting trustees, the members of the committee shall be entitled to compensation and expenses as provided above in connection with the voting trust.

The reorganization committee shall have, subject to any requirements of law and the requisite approval of the court and this Commission, full and plenary discretionary power to take all such action and to enter into such arrangements, financial and otherwise, as they may deem necessary or advisable in order to consummate and carry into execution the plan or any modification thereof; to create a new corporation if a new corporation be deemed advisable; to supervise and determine the form of instruments necessary to transfer the property of the debtor to the reorganized corporation; to employ and fix the compensation of mortgage trustees, depositaries, counsel, and others whose services they may employ in the execution of their powers; to determine the form and provisions, so far as not otherwise herein specifically provided, of the certificate of incorporation of the new company, if a new cor-

poration is to be formed, and its bylaws, or to determine the necessary amendments to the debtor's certificate of incorporation and its bylaws, the new bonds and the mortgages and trust agreements under which the same shall be issued, the stock certificates, and any other instruments deemed by the reorganization committee to be necessary or proper in connection with the plan; to provide the method by which creditors and other interested parties may participate in the plan; and to do all other acts in their discretion advisable for carrying out the plan.

The court shall, before they are put in use, approve the articles of incorporation, amendments to articles of incorporation, bylaws, mortgages, trust agreements, bonds, securities, stock certificates, and the escrow agreement for the new stock.

Except as otherwise expressly provided in the plan, the reorganization committee may act by a majority at a meeting, or by unanimous consent in writing without a meeting; they may, from time to time, delegate to others any power or discretion conferred upon them by the plan; and its members shall not be liable for any action taken by them in good faith or by any person employed by them in good faith, except for their respective individual malfeasance or willful neglect.

The reorganization committee shall not be authorized to solicit authorizations to represent security holders, or solicit the deposit of securities for purposes other than exchange, except upon approval by this Commission of the terms of such solicitation, pursuant to section 77 (p) of the Bankruptcy Act.

Acceptance of the plan shall include acceptances of the new bonds, mortgages, stock certificates, and all instruments necessary and appropriate to the carrying out of the plan, other than the orders of the court and this Commission, to the same effect as though the terms of such instruments were set out in full herein.

The method by which creditors and any other parties in interest may, after confirmation of the plan by the court, participate therein shall be determined by the reorganization committee with the approval of the court, and notice thereof duly given.

Provision permitting sale of debtor's property.—R. If so ordered by the court, the plan, after it has been found fair and equitable and confirmed by the court, may be executed by the sale or sales, at not less than fair upset prices, to be fixed by the court, of all or any part of the property of the debtor and the secondary debtor, all on such conditions and in such manner as the court may direct. Upon any such sale or sales, the property and assets offered for sale may be purchased for the benefit of the new company by the reorganization committee, and in that event there shall be applied

on account of the purchase price the distributive share of the proceeds of such sale of all securities the holders of which shall have assented to the plan, and of the securities, though not assenting to the plan, of all classes which shall have accepted the plan. If the property of the debtor or secondary debtor, or both, so offered for sale should be sold to others than the reorganization committee, the plan herein approved shall be deemed inoperative except insofar as provision is made therein for the sale of the properties as may be ordered by the court.

In the event of any such sale to the reorganization committee, it may in its discretion sell all or any portion of the new securities distributable under the plan in respect of securities of any creditor, if neither such creditor nor the class to which such creditor belongs shall have accepted the plan, provided that creditors, in a class which shall not have accepted the plan, and who themselves shall not have accepted the plan, shall have the right, if they shall so notify the committee within a period of 30 days after the confirmation of the sale to assent to the plan and receive the securities allocated to them under the plan in lieu of their aliquot share of the proceeds of such sale. The proceeds of sale of securities, with the approval of the court, and any other funds which in the judgment of the reorganization committee are available among the assets of the debtor's estate and are not necessary for the working capital requirements of the new company, or to pay any of the obligations under the plan, may be used to pay the portion of the purchase price payable in cash on any such sale of the properties.

Taxes due to the United States.—S. The debtor, as reorganized, or the transferee of the property, shall assume the liability for, and shall pay in full in due course, any and all taxes due to the United States from the debtor or the trustees for any taxable period prior to the date of confirmation of a plan of reorganization, without requiring proof thereof in this proceeding and without prejudice by reason of not having been proved herein, subject, however, to the statutes of limitation normally applicable to the assessment and collection of such taxes, provided, however, that the liability of the reorganized company for any taxes which are the subject of litigation on the date of the confirmation of the plan of reorganization, or which may become the subject of litigation on any date thereafter and prior to the expiration of the applicable statute of limitations, shall be determined pursuant to law, and provided, further, however, that this provision shall not be deemed to preclude either the debtor, the trustees, or the reorganized company from contesting the merits of any such tax in the manner provided by law.

Construction of plan.—T. The construction of the plan by the court shall be final and conclusive. The court may cure any defect, supply any omission, or reconcile any inconsistency, in such manner or to such extent as may be necessary or expedient to carry out the plan effectively.

Additiondl Clauses from Commission's Order of June 14, 1943

In addition to the provisions of the plan approved hereinbefore shown, the Commission's order approving the plan also ordered—

(1) That the authorization and approval herein granted by this Commission are upon the condition that the journal entries covering the necessary accounting adjustments under the order will be submitted to this Commission for approval before they are recorded on the books of the new company under the plan of reorganization herein approved.

(2) That nothing herein contained shall be, or be construed as, a grant of authority for the issue of any securities, assumption of obligations, transfer of any property, sale, consolidation, or merger of the debtor's property, or pooling of traffic pursuant to either the Bankruptcy Act or the Interstate Commerce Act, except as provided herein, or until further action by this Commission upon confirmation of the plan by the court; and

(3) That, except as aforesaid, the petitions for modification of the report and order of July 13, 1942, be, and they are hereby, denied.

PLAN OF REORGANIZATION

Change Made by the Court in the Plan of Reorganization Approved by the Commission

On September 16, 1943 the court entered an order directing the trustees to purchase the Rio Grande Junction bonds at par and accrued interest at 5 percent per annum from June 1, 1935 from all bondholders tendering their bonds for purchase and the trustees have given notice pursuant to the order that on and after November 1, 1943 they will purchase such bonds at said price, but with accrued interest terminating on that date.

In the above-described order the court referred to the provision of the plan approved by the Commission providing that the provisions of the plan with respect to the Rio Grande Junction bonds should be considered as separable. It appearing that the above action of the court was taken pursuant to such provision, and that the plan in so far as it provides treatment for the Junction bonds will not be placed in effect, no submission will be made of the remainder of the plan to the Junction bondholders.

INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002[1]

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

Submitted December 7, 1938. Decided July 11, 1939

Plan of reorganization for the Denver & Rio Grande Western Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, approved.

F. C. Nicodemus, Jr., and *William V. Hodges* for debtors.

Henry W. Anderson, George D. Gibson, Leighton H. Schurbeck, Oscar R. Ewing, Harry Hoffman, Edgar J. Goodrich, Mildred E. Reeves, John B. Marsh, Edward E. Watts, Jr., Fred N. Oliver, Karl Michelet, Charles J. Nasmyth, John E. Benton, Clyde S. Bailey, Simon Fleishman, Clarence R. Freeman, Stanley Marsh, Robert McKinney, W. Heyward Myers, Jr., Philip B. Fisher, William Clarke Mason, Edwin S. S. Sunderland, Thomas O'G. FitzGibbon, Malcolm Fooshee, Daniel Willard, Jr., Gerald Hughes, William A. W. Stewart, Harry L. Umbarger, Erskine R. Myer, James B. Alley, C. C. McChord, C. M. Clay, W. Meade Fletcher, Jr., Arthur A. Gammell, W. C. Roper, Jr., H. Struve Hensel, Frederick W. Wood, Rodney J. Bardwell, Jr., H. H. Larimore, Russell L. Dearmont, W. M. Dyer, Carl Giessow, C. O. Heinley, Paul B. Cromelin, and *H. C. Clark*, for interveners.

Report of the Commission

BY THE COMMISSION:

Exceptions to the report[2] proposed by the examiner were filed, and oral argument was heard. Our conclusions differ from those of the examiner.

[1] This report also embraces reorganization and consolidation of the Denver & Salt Lake Western Railroad Company, secondary debtor, the Denver & Salt Lake Railway Company, the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company, none of the last three having filed petitions under section 77.

[2] Previous reports, 212 I. C. C. 105 and 709, 217 I. C. C. 101, and 224 I. C. C. 574. Orders entered without report (other than order permitting interventions) January 21, August 8, and September 4, 1936; January 9, April 12, May 26, and October 27, 1937; and May 26 and November 28, 1938.

The Denver and Rio Grande Western Railroad Company and The Denver and Salt Lake Western Railroad Company, hereinafter referred to as the Denver and the Salt Lake Western, or the debtor and the secondary debtor, respectively, on November 1, 1935, filed petitions with the District Court of the United States for the District of Colorado, stating that they were unable to pay their debts as they matured and that they desired to effect a plan of reorganization under section 77 of the act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States," as amended. On the date of the filing of the petitions the court entered orders approving the petitions as properly filed and, among other things, pending the appointment of trustees, authorized and directed the debtor to operate and maintain both properties, under the supervision of the court. Copies of the petitions and the orders thereon have been transmitted to us by the clerk of the court. In like manner we have received lists of all known creditors and stockholders of the debtors, together with copies of orders of the court determining the time within which and the manner in which the claims and interests of the creditors and stockholders may be filed or evidenced and the division of creditors and stockholders into classes for the purpose of the plan and its acceptance. These and other documents similarly received are now of record in the proceeding before us.

By order entered November 18, 1935, the court appointed Wilson McCarthy and Henry Swan trustees of the debtor, and these appointments were later ratified by division 4. By order entered December 19, 1935, the court appointed Raymond L. Sauter trustee of the secondary debtor, and this appointment was likewise ratified. Upon petition of the debtors, the court on April 29, 1936, entered an order extending the time for filing a plan of reorganization from the due date under section 77(d) of the act to and including August 1, 1936. On July 29, 1936, a "Proposed Plan of Consolidation and Reorganization as of January 1, 1937" was filed with the court and with us by the debtors. The plan embraced the Denver, the Salt Lake Western, the Denver & Salt Lake Railway Company, the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company.

By the provisions of section 77(d), after the filing of a plan, unless such plan is found to be *prima facie* impracticable, we are required to hold public hearings thereon, at which any interested party may be heard, and to render a report and order in which we may either approve or refuse to approve a plan. The plan approved may be different from any which has been proposed but it must in our opinion, among other things, be fair and equitable, afford due

recognition to the rights of each class of creditors and stockholders, not discriminate unfairly in favor of any class of creditors or stockholders, conform to the law of the land regarding the participation of the various classes of creditors and stockholders, and be compatible with the public interest. After due notice, hearings were held in October 1936 and in February, April, and June, 1937. At the hearing on June 15, 1937, a plan of reorganization embracing the companies covered by the debtor's plan was filed by the Insurance Group committee, an intervener, of which George S. Van Schaick was chairman. Besides this group the interveners included the trustees under certain mortgages, the Untermyer family group, the Security Research Bureau, the Chase National Bank of the City of New York, the Railroad Credit Corporation, several chambers of commerce and boards of trade, the Reconstruction Finance Corporation hereinafter called the Finance Corporation, and others. Briefs were filed.

Classes of creditors and stockholders.—The district court, by order entered November 23, 1936, divided the claims and interests of the creditors and stockholders as follows: Class 1, common stock; class 2, preferred stock; class 3, claims entitled to priority under section 77 (n); class 4, claims which would have been entitled to priority over existing mortgages or other liens if a receiver in equity had been appointed for the property; class 5, claims not included in classes 3 and 4, which are entitled to priority by virtue of the laws of any State or of the United States; class 6, bonds issued under the consolidated mortgage of the Denver & Rio Grande Railroad Company dated July 15, 1886, assumed by the debtor; class 7, bonds issued under the first-trust mortgage of the Rio Grande Western Railway Company, dated July 1, 1889, assumed by the debtor; class 8, bonds issued under the first consolidated mortgage of the Rio Grande Western Railway Company, dated April 1, 1899, assumed by the debtor; class 9, bonds issued under the first mortgage of the Rio Grande Junction Railway Company dated December 1, 1889, assumed by the debtor; class 10, bonds issued under the debtor's refunding and improvement mortgage dated February 1, 1924, and bonds issued under the improvement mortgage of the Denver & Rio Grande Railway Company, dated June 1, 1888, which may be held to be pledged under the aforesaid refunding and improvement mortgage; class 11, bonds issued under the debtor's general mortgage dated February 1, 1924, and bonds issued under the improvement mortgage of the Denver & Rio Grande Railroad Company which may be held to be pledged under the aforesaid refunding and improvement mortgage; class 12, secured notes of the debtor held by the Railroad Credit Corporation,

the Chase National Bank of the City of New York, and the Finance Corporation, and the debt of the Salt Lake Western, represented by the debtor's demand note which was pledged by the Salt Lake Western as security for a loan from the Finance Corporation; and class 13, all other claims not coming within any of the aforesaid specific classifications.

Claims evidenced by equipment-trust indentures and leases, or equipment-trust certificates secured thereby, were not classified, in view of the following provision of section 77 (j):

> The title of any owner, whether as trustee or otherwise, to rolling stock equipment leased or conditionally sold to the debtor, and any right of such owner to take possession of such property in compliance with the provisions of any such lease or conditional sale contract, shall not be affected by the provisions of this section.

The amount of stock, bonds, secured notes, and unsecured claims outstanding will be shown in detail later.

The Properties

The Denver's principal eastern termini are Denver and Pueblo, Colo., at each of which points connection is made with the Atchison, Topeka & Santa Fe Railway and the Colorado & Southern Railway. At Denver connection is also made with the Chicago, Burlington & Quincy Railroad, the Chicago, Rock Island & Pacific Railway, and the Union Pacific Railroad; at Pueblo, also with the Missouri Pacific Railroad, which is the Denver's main outlet to the east.

On the west the main line of the Denver passes through Salt Lake City and terminates at Ogden, Utah. Connection is made with the Union Pacific at each point; at Salt Lake City the Denver also connects with the Western Pacific Railroad and at Ogden with the Southern Pacific. The interchange with the Western Pacific is more important than that with any other western connection.

The road owned by the Denver consists of 1,256.6 miles of main line and 1,094.9 miles of branch lines. Operated under lease are the Rio Grande Junction Railway (hereinafter called the Junction) extending from Rifle to Grand Junction, Colo., 62.1 miles, the Goshen Valley Railroad, a branch line 8.8 miles in length, and the Salt Lake Western, extending from Dotsero, on the Denver, to Orestod on the Denver & Salt Lake Railway (hereinafter called the Salt Lake), 38.1 miles. Including these leased lines, the Denver operates approximately 1,357 miles of main lines and 1,104 miles of branch lines. Approximately 771 miles of narrow-gage lines are included in the operated mileage.

In addition to the above-mentioned mileages, the Denver operates over the Salt Lake, between Denver and Orestod, 128.6 miles. This line, together with the Salt Lake Western, constitutes the Dotsero cut-off route. The Salt Lake's ownership embraces the line extending from Utah Junction, near Denver, to the western terminus at Craig, Colo., 220.2 miles. For its Denver terminal, the Salt Lake uses, under a lease, the facilities of the Northwestern Terminal Railroad Company. The Salt Lake derives no revenues from the through traffic moving over the cut-off, since all such traffic is handled by the Denver.

The present Denver Company was organized on November 17, 1920, succeeding the Denver & Rio Grande Railroad Company, organized in 1908. The former corporation acquired the property of the Rio Grande Western Railway Company (hereinafter called the R. G. Western), owning the line extending west from Crevasse, Colo., to Ogden, Utah, and that of the Denver & Rio Grande Railroad Company of 1886, owning all lines east of Crevasse except the Junction line. The 1908 company assumed obligation in respect of bonds issued under the R. G. Western's first-trust mortgage of 1889 and its first consolidated mortgage of 1899. It likewise assumed obligation in respect of bonds issued under the first consolidated mortgage made by the Denver & Rio Grande of 1886.

The Denver & Rio Grande Railroad Company of 1908 also assumed the obligations of the predecessor companies with respect to securities issued by the Western Pacific Railway Company. It also issued bonds under new mortgages, viz., the first and refunding mortgage and the adjustment mortgage. Default in the payment of interest on the first-mortgage bonds of the Western Pacific led to a deficiency judgment against the Denver of 1908 and ultimately to the creation of the present Denver Company, which assumed obligation for all the bonded debt of the former company. It issued 309,000 shares of capital stock to the Western Pacific Railroad Corporation, a new company formed for the purpose of controlling the Western Pacific Railroad Company. See *Denver & R. G. W. R. Co. Stock*, 70 I. C. C. 102. Later a half interest in this stock was sold to the Missouri Pacific Railroad Company for $9,000,000. *Acquisition of Denver & R. G. W. Common Stock*, 90 I. C. C. 161.

Operation of the Junction property under lease began in 1890 and continues under the same lease. It originally provided for the guaranty of the Junction's first-mortgage bonds of 1889 by the Denver of 1886 and the Colorado Midland Railway Company. The latter ceased operation in 1918. These bonds constitute an obligation of the present debtor. The debtor owns $906,000 of the Junc-

tion's refunding junior bonds, issued in 1929, and $2,000,000, par value, of the Junction's capital stock.

The debtor owns the entire capital stock of the Goshen Valley, having a par value of $50,000.

Foreclosure proceedings were instituted against the Denver in 1922 as a result of default in the payment of interest on the first and refunding mortgage and the adjustment-mortgage bonds, issued in 1908, which were undisturbed in the previous reorganization. A receiver was appointed and the property was sold at auction to the reorganization managers in accordance with the plan of June 15, 1923. By deed dated December 1, 1924, the property was conveyed back to the company. See *Denver & R. G. W. R. Co. Reorganization*, 82 I. C. C. 745 and 90 I. C. C. 141. The aforesaid first and refunding mortgage bonds, purporting to represent a lien on a substantial amount of equipment, were exchanged 60 percent in new general-mortgage bonds and 40 percent in preferred stock.

The Salt Lake was incorporated on November 3, 1925, and on January 1, 1927, acquired the properties of the Denver & Salt Lake Railroad Company at foreclosure. *Denver & S. L. Ry. Co. Reorganization*, 117 I. C. C. 397.

The latter company had by similar means acquired the properties of the Denver, Northwestern & Pacific Railroad Company in 1913, and has extended the line from Steamboat Springs to Craig, approximately 41 miles. Owing to difficult operating conditions, the carrier went into receivership in 1917. Between that time and the reorganization of 1925-26, the Moffat Tunnel project was carried out by the Moffat Tunnel Commission, which manages the property of the Moffat Tunnel Improvement District. The tunnel is 8.9 miles in length, and the portion built for railroad use is leased to the Salt Lake. Under the terms of this lease the Salt Lake is obligated to pay 66⅔ percent of the principal and interest of the Moffat Tunnel bonds, the cost of maintaining the railroad tunnel, and certain other amounts. The Moffat Tunnel Improvement District, pointing out that it has no relations with the Denver Company and that a consolidation of the Salt Lake with the Denver in connection with the reorganization would cause the former, now solvent, to lose its corporate identity, contends that the Salt Lake has no right to assign or sublet the lease of January 6, 1926, without the consent of the tunnel district. It suggests that if the present lease is to be canceled provision should be made for a new lease with the consolidated company under which the tunnel district will receive the same measure of security that it now has from the present lessee.

With the purpose of developing a western outlet, the Salt Lake

organized the Salt Lake Western, which completed the construction of its line from Bond, near Orestod, to Dotsero on June 15, 1934, pursuant to the certificate issued by the Commission in *Denver & S. L. W. R. Co. Construction*, 154 I. C. C. 51 and 175 I. C. C. 535. All the capital stock of the Salt Lake Western was owned by the Salt Lake. Along with the granting of authority for the construction of the Salt Lake Western line, the Commission authorized the Denver to acquire control of the Salt Lake by purchase of capital stock; *Denver & S. L. Ry. Co. Control*, 170 I. C. C. 4, and 175 I. C. C. 542. Later, in *Denver & R. G. W. R. Co. Operation*, 189 I. C. C. 129, it authorized the Denver to operate the line of the Salt Lake Western under lease and to operate under trackage rights over the line of the Salt Lake between Utah Junction and Orestod. The agreements made by the carriers in respect of these matters are described in *Denver & S. L. W. R. Co. Construction, supra*. The agreement relating to the Salt Lake Western provides that, contingent upon the transfer of that company's stock or mortgage bonds to the Denver, the latter would finance the construction of the cutoff. The terms of the lease were also set forth. In accordance with this agreement, $3,631,000, par value, of the stock of the Salt Lake Western was transferred to the Denver. The Salt Lake Western has issued no bonds.

The total amount of stock of the Salt Lake acquired by the Denver is 49,540 shares of no-par value. Stock remaining outstanding in the hands of the public aggregates 460 shares. All the stocks of the Salt Lake and the Salt Lake Western owned by the Denver, together with various other securities, are pledged with the Finance Corporation as collateral security for loans for the financing of the construction project, the acquisition of the Salt Lake stock, and the payment of interest, taxes, and maturing equipment-trust certificates.

The investment in road and equipment of the several corporations, as shown on the consolidated balance sheet of December 31, 1936, was as follows: $211,635,295 for the Denver, $5,328,626 for the Junction, $3,659,578 for the Salt Lake Western, $503,890 for the Goshen Valley, and $17,059,350 for the Salt Lake, a total of $238,186,739. Including all investments, the grand total was $240,145,360. As of December 31, 1935, the grand total was $238,759,511.

In connection with the above-stated amounts appearing on the consolidated balance sheet, the debtor introduced an analysis of capitalizable assets, based on data furnished to us in other proceedings in connection with applications for authority to issue securities. The result arrived at is $241,295,293, which is described

as the grand total capitalizable investment as of December 31, 1935.

The report of the Bureau of Valuation dated March 1, 1937, filed in this proceeding by direction of division 4, sets forth various elements of rate-making value in respect of the Denver property and that of its subsidiaries, as of December 31, 1935. For the Denver the original cost is $142,800,512, the cost of reproduction new $168,729,747, the cost of reproduction new, less depreciation, $115,467,756, the value of lands and rights $5,428,159, and the amount of working capital $2,473,400. For the Salt Lake the corresponding amounts are $17,549,593, $19,934,420, $14,462,618, $91,854, and $287,000. For the Junction, omitting working capital, the amounts are $3,401,673, $4,100,037, $3,409,074, and $60,330, for the Goshen Valley $499,441, $308,078, $270,756, and $1,908, and for the Salt Lake Western $3,547,081, $3,920,258, $3,880,723, and $7,219, respectively. The totals for the system are original cost $167,798,300, reproduction cost new $196,992,540, reproduction cost new, less depreciation, $137,490,927, land and rights $5,589,470, and working capital $2,760,400.

The sum of the last three amounts is $145,840,797, and if net additions and betterments during 1936 be added thereto the total would be $147,717,268. On the basis of original cost the total as of December 31, 1936, would be $178,024,641.

Securities of the Denver which are owned by the Western Pacific Railroad Corporation include 150,000 shares (50 percent) of no-par common stock, $2,070,000, par value, of preferred stock, $1,000,000 of refunding and improvement mortgage bonds, $3,751,875 of general-mortgage bonds, $364,000 of R. G. Western first consolidated mortgage bonds, and $10,000 of the first consolidated mortgage bonds of the Denver of 1886. Most of these securities are pledged, the Denver's common stock being deposited with the Finance Corporation as security for a loan to the Western Pacific Railroad Company.

Securities of the Denver which are owned by the Missouri Pacific include 150,000 shares (50-percent) of the no-par common stock, $608,800, par value, of the preferred stock, and $1,000,000 of refunding and improvement mortgage bonds. All the common and preferred stock is pledged with the Railroad Credit Corporation.

Proceedings for the reorganization of the Western Pacific and Missouri Pacific under section 77 are pending before us and the courts.

Present capital structure.—The Denver's balance sheet of December 31, 1936, shows common stock (300,000 shares) as $62-

457,540, preferred stock $16,445,600, funded debt unmatured $76,707,500, trustees' certificates $650,000, and grants in aid of construction $800,313. Total current assets were $8,025,321 and total current liabilities were $69,729,998, the latter including $12,966,372 of interest matured unpaid and $45,317,500 of funded debt matured unpaid. Corporate surplus was shown as a deficit of $2,309,419 in liabilities.

The debtor's common stock is held under a trust agreement dated February 1, 1924, voting-trust certificates being held in equal amounts by the proprietary companies. The preferred stock is entitled to dividends at the rate of 6 percent per annum, cumulative from February 1, 1924, and to $100 a share in a dissolution of the company, in preference to the common stock. No dividends have ever been paid on this stock. Equipment-trust certificates were outstanding as follows: Series A, $600,000; series B, $575,000; and series C, $630,000. Pursuant to the authority granted by division 4 in *Denver & R. G. W. R. Co. Trustees' Equipment Trust Certifs.*, 221 I. C. C. 291, $2,175,000 of series-D certificates were issued by the trustees in 1937. The equipment-trust certificates outstanding on June 30, 1938, consisted of $345,000 of series B, $420,000 of series C, and $2,030,000 of series D, a total of $2,795,000.

The Denver's long-term funded debt outstanding as of December 31, 1936, is briefly described as follows: Junction first-mortgage 5's due December 1, 1939, principal amount $2,000,000, unpaid interest $158,333; R. G. Western first-trust 4's due July 1, 1939, principal amount $15,190,000, unpaid interest $1,215,200; D. & R. G. first consolidated mortgage bonds due January 1, 1936, consisting of $34,125,000, principal amount, of 4's, with unpaid interest of $3,412,500, and $6,382,000 of 4½'s, with unpaid interest of $717,975; R. G. Western first consolidated 4's due April 1, 1949, principal amount $15,080,000, unpaid interest $1,357,200; the Denver's refunding and improvement mortgage bonds, consisting of series A, due October 1, 1974, principal amount $2,000,000, unpaid interest $270,000, and series B, due April 1, 1978, principal amount $12,000,000, unpaid interest $1,350,000; and the Denver's general-mortgage 5's, due August 1, 1955, principal amount $29,808,000, unpaid interest $12,544,200, of which $7,452,000 represents noncumulative interest to February 1, 1929, included in the total claim as stated by the trustee under the mortgage.

In addition to the foregoing there have been issued and pledged $906,000 of the Junction's refunding 5's, $10,000 of R. G. Western first-trust 4's, $1,395,000 of R. G. Western consolidated 4's, $1,445,000 of D. & R. G. first consolidated 4's, and $10,481,000 of the

Denver's refunding and improvement mortgage 5's. A statement of all securities pledged for short-term loans appears later.

The debtor introduced statements setting forth its views as to what properties are subject to the respective first liens of the several mortgages. The Junction's first mortgage and refunding mortgages represent first and second liens, respectively, on the 62.1 miles of line owned by this company. No equipment is involved with these mortgages. The R. G. Western first-trust mortgage represents a first lien on 314 miles of main line and a total of 415 miles of line, together with equipment having a ledger value, less depreciation, of $17,637, as of December 31, 1936. The R. G. Western first consolidated mortgage represents a second lien on that property and a first lien on approximately 283 miles of branch lines in Utah, the entire capital stock of the Utah Fuel Company, and equipment having a ledger value, less depreciation, of $681,191. The D. & R. G. first consolidated mortgage represents a first lien on 875 miles of standard-gage lines and 683 miles of narrow-gage lines in Colorado, and on equipment having a ledger value, less depreciation, of $4,708,523, as considered by the debtor. The Denver's refunding and improvement mortgage represents a first lien on 85 miles of standard-gage and 34 miles of narrow-gage branch lines in Colorado and Utah, a junior lien on all other lines owned, and a first lien on equipment having a ledger value, less depreciation, of $7,268,622, according to the debtor. In addition, there are pledged under this mortgage the shares of stock, less directors' qualifying shares, of the Junction, the Denver Union Terminal Company, the Pueblo Union Depot & Railroad Company, and the Salt Lake City Union Depot & Railroad Company owned by the debtor, together with $906,000 of the Junction's refunding bonds. The Insurance Group committee argues that a portion of the above-mentioned equipment, having a depreciated value of $1,333,252, should be allocated to the first lien of the D. & R. G. first consolidated mortgage rather than to that of the refunding and improvement mortgage, as the trustee of the latter contends. This question will be discussed later. The Denver's general mortgage represents a lien generally upon the property securing the refunding and improvment mortgage but junior thereto. The Denver's investment in the stocks and bonds of the R. G. Western, the Salt Lake, the Salt Lake Western, and the Goshen Valley, together with advances, aggregates $15,060,147. Its short-term secured debt, as of December 31, 1936, consisted of loans from the Finance Corporation totaling $10,691,850, upon which the interest unpaid amounted to $628,108, a balance of approximately $300,000 due on a loan of $500,000 from the Railroad Credit Corporation, and a demand

note for $1,500,000 given to the Chase National Bank of the City of New York upon which $53,948 of interest was computed by the debtor and the committee up to December 31, 1936.

The collateral pledged as security for the Denver's note to the Finance Corporation in the amount of $7,581,000 and the Salt Lake Western's note in the amount of $3,110,850 (the latter also secured by a demand note of the Denver for $3,182,150) consists of the following securities: $10,000 of R. G. Western first-trust 4's, $1,395,000 of R. G. Western first consolidated 4's, $783,000 of D. & R. G. first consolidated 4's, $4,385,000 of the Denver's refunding and improvement 5's, $1,266,000 of the Salt Lake's income 6's, 49,546 shares of the Salt Lake's capital stock, 36,310 shares of the Salt Lake Western's capital stock, 56,700 shares (100 percent) of the capital stock of the Denver–Colorado Springs Pueblo Motor Way, Incorporated, 1,352 shares (100 percent) of the capital stock of Rio Grande Motor Way, Incorporated, 500 shares (100 percent) of the capital stock of the Goshen Valley Railroad Company, and $1,777,000 of bonds of the Rio Grande Southern Railroad Company. The above-stated shares of the motor companies' stock include additional shares deposited in May 1937 in accordance with the supplemental certificate issued by division 4 in *Denver & R. G. W. R. Co. Reconstruction Loan*, 221 I. C. C. 107. The notes to the Finance Corporation are further secured by a junior lien on the collateral pledged with the Railroad Credit Corporation and the Chase National Bank, viz, $662,000 of D. & R. G. first consolidated 4's and $6,096,000 of the Denver's refunding and improvement 5's, respectively. The Credit Corporation is further secured by pledge of the debtor's distributive share of the funds collected under the marshaling and distributing plan and by a junior lien on the collateral pledged with the Finance Corporation. The motor companies above referred to represent an investment of $172,300 by the Denver. Operating as feeders to the railroad, they report substantial earnings in practically every year since 1927.

Unsecured general claims against the debtor aggregated approximately $440,000. An undetermined amount falls within the six-months rule. To the extent these unsecured creditors are not paid off currently they would be offered, under the debtor's plan, participating preferred stock at the rate of one share for each $100 of claims.

The debtor stated that, during the 11-year period following the previous reorganization, more than $30,000,000 was expended on the property for additions and betterments, while the amount of equipment obligations was reduced by $1,925,000 and the amount of refunding and improvement mortgage bonds outstanding was

increased by $12,000,000, due, however, chiefly to the retirement of bonds matured on June 1, 1928. For the payment of interest and taxes not earned in 1931, 1932, and 1933, loans of $3,950,000 from the Finance Corporation and of $500,000 from the Railroad Credit Corporation were obtained. Additional loans from the Finance Corporation, in the amounts of $3,631,000 and $3,110,850, were obtained for the Salt Lake Western construction and the purchase of Salt Lake stock, respectively. The bank loan of $1,500,000 was also applied to the latter purpose. Including $1,042,559 of Salt Lake income bonds, together with advances, the Denver's investment in the cut-off route amounts to $12,526,376.

Division 4, by orders entered on January 29 and December 23, 1937, and March 1, 1938, authorized the trustees of the debtor to issue and sell trustees' certificates of series C not exceeding $1,800,000 in amount, series D not exceeding $3,200,000, series E not exceeding $1,800,000; and series F not exceeding $2,000,000. *Denver & R. G. W. R. Co. Trustees' Certificates*, 217 I. C. C. 796, and 224 I. C. C. 336 and 596. The series-C certificates were paid at maturity. The series-F certificates were never issued. By order entered January 24, 1939, division 4 authorized the trustees to issue and sell $5,000,000 of series-G certificates for the purpose of paying a like amount of outstanding certificates at maturity, early in February, 1939. The series-G certificates bear interest at the rate of 3½ percent, mature on February 1, 1942, and are redeemable on any interest-payment date at par and accrued interest. 230 I. C. C. 609.

The Denver's obligation in respect of the securities of the three terminal companies, mentioned above in connection with the refunding and improvement mortgage bonds, is shown in the agreements made for joint use of the terminals. Copies of the balance sheets and income accounts of the terminal companies are of record herein. The debtor's trustees have advised us that they and the trustees of the Western Pacific were unable to pay the $557,000 of first-mortgage bonds of the Salt Lake City Union Depot & Rail-Road Company which became due on November 1, 1938, and for which the Denver and the Western Pacific are jointly liable under a four-party agreement dated November 1, 1908. This agreement has not been adopted by the trustees of the debtors, but they have met the interest and sinking-fund payments on the terminal bonds when due. They propose to refinance the major part of the matured bonds with the aid of the Finance Corporation.

The unpledged securities then owned by the debtor and its subsidiaries included $46,000 of certificates issued by the receiver of the Rio Grande Southern Railroad Company and $850,000 of

United States Treasury bonds. The debtor stated that these were the only securities in the list which had any realizable value. The treasury bonds have since passed out of the debtor's possession.

At the hearing it was stated that in connection with the Denver's reorganization of 1924 there were still issuable $108,900 of general-mortgage bonds and $15,600 of preferred stock in exchange for old securities. There were still issuable by the Salt Lake, in connection with its reorganization plan of 1925, approximately $20,200 of bonds and 30 shares of stock, and $21,806 in cash was being held for payment to nonassenting bondholders of the predecessor company. Counsel for the trustees have advised us that as of April 30, 1939, the securities of the Denver held for conversion of old securities consisted of 124 shares of preferred stock and $24,950, principal amount, of general-mortgage bonds. It appears that in the final decree of sale of the property in 1924 the holders of the old refunding bonds and adjustment bonds are entitled to their distributive share in cash (estimated at about $8,568) and that the refunding-mortgage trustee has sought an order of the court in the old receivership proceeding to authorize such settlement. The outcome of this matter cannot be determined at this time.

As has been stated, the capitalization of the Salt Lake Western consists of common stock, all of which is owned by the debtor. The securities of the Salt Lake outstanding consist of 50,000 shares of common capital stock of no-par value, of which 49,540 shares are owned by the debtor, and $12,500,000 of funded debt unmatured. The latter amount is composed of $1,500,000 of first-mortgage 4-percent bonds due January 1, 1950, and $11,000,000 of 6-percent income-mortgage bonds due January 1, 1960, of which $1,266,000 are owned by the debtor.

The $2,217,000 of first-mortgage 5-percent bonds of the Northwestern Terminal Railroad Company are involved to the extent that under the terms of the lease the Salt Lake pays a portion or all of the interest on such bonds, according to the amount of the railway revenues, and in the event the Salt Lake is consolidated with any other railroad the new company shall pay the full 5-percent interest. Although the debtor's plan proposes that the use of these terminal facilities be discontinued and that the debtor's terminal facilities in Denver be used by the carriers proposed to be consolidated, it provides in its plan for the possible issue of new first-mortgage bonds to refund the terminal-company bonds outstanding.

Combining and summarizing the capital structures of the debtor and its subsidiaries as of December 31, 1936, and omitting intercompany holdings and securities pledged, the total long-term and

short-term debt, including unpaid interest,[3] was $157,056,723, the amount of preferred stock was $16,445,600, par value, and the common stock outstanding consisted of 300,460 shares of no-par value. The total amount of fixed interest charges for this capitalization was $5,835,392 per annum, the contingent interest charges $584,040 per annum, and the preferred-stock dividend requirements $986,736 per annum, all based on the principal amounts outstanding, without consideration of the $14,293,464 of accumulated unpaid interest on secured obligations and the $12,745,340 of accumulated dividends on the preferred stock.

Subsequent to December 31, 1936, the capital structure was changed by the issue of additional equipment-trust certificates and trustees' certificates, as has been shown, and by the further accumulation of unpaid interest on funded debt and loans.

The debtor presented a pro-forma balance sheet for the combined companies as of December 31, 1936, based on their present investments, with intercompany eliminations and adjustments. The capital liabilities shown are those proposed in the debtor's plan. According to this set-up the assets of the new company would consist of total investments of $228,541,993, total current assets of $9,400,095, total deferred assets of $8,495, and total unadjusted debits of $1,443,351. On the liability side, the total capitalization is shown as $119,454,419, including the proposed no-par participating preferred stock at $1 a share. The amount $113,298,420 is set up as reorganization adjustment of capital, bringing the total capital liabilities to $232,752,839. Total current liabilities are $4,277,141, total deferred liabilities $363,210, and total unadjusted credits $2,000,744. Because of the reorganization adjustment made, no corporate surplus appears.

Traffic and earnings.—As shown by traffic-density charts for the years 1935 and 1936, the Denver's freight traffic is fairly uniform in total amount between Denver and Walsenburg, between Pueblo and Dotsero, between Dotsero and Helper, and between Helper and Salt Lake City, the density increasing in this order of districts. East of Helper the movement is predominantly eastbound and between Helper and Salt Lake City predominantly westbound. Most of the coal tonnage, constituting the largest single item of traffic handled, originates around Helper and moves west. Except on small portions of line the traffic of the narrow-gage lines is generally less than 50,000 net ton-miles per mile of road a year. Of the total through traffic in 1935, approximately 40 percent moved over the cut-off. Some of this traffic was created by the opening

[3] Except $7,452,000 of contingent interest on the general mortgage bonds outstanding.

of the new route and therefore does not represent an actual diversion from the old route via Pueblo.

Of the Denver's freight revenues in 1936, 19 percent was derived from products of agriculture, 6 percent from products of animals, 29 percent from products of mines, 6 percent from products of forests, 34 percent from manufactures and miscellaneous, and 6 percent from less-than-carload freight. The commodities constituting the chief items of traffic move, in general, over all the lines. The traffic originating on the principal branches was described in detail. Compared with the revenues of 1929 the largest relative declines have been in the products of mines and in less-than-carload freight. Compared with 1932 the total revenues in all main freight groups have increased, particularly in products of mines and forests, in manufactures and miscellaneous, and in less-than-carload freight.

The Denver's total carload traffic decreased from 330,250 cars in 1929 to 185,111 cars in 1933, then increased each year to a total of 276,968 cars in 1936. The overhead or bridge traffic handled during the year ended June 30, 1935, aggregated 1,402,477 tons, yielding revenues of $5,754,924. In the opinion of the debtor, 4 or 5 years will be required for the full development of the cut-off route. The traffic handled over it is highly competitive in character.

A record of the Denver's interchange of freight with its principal connections from 1924 to 1935 shows that the tonnage received from the Western Pacific exceeds that received from any other line, while the tonnage delivered to the Missouri Pacific exceeds that delivered to any other. In the reverse movement these roads are also important connections. A large tonnage of freight is interchanged with the Union Pacific and Southern Pacific. The Denver's interchange with the Salt Lake is small compared to the interchange with the trunk lines.

Traffic reported as being handled by the Denver, following the opening of the cut-off route, includes that handled over the lines of the Salt Lake Western and the Salt Lake under the operating agreements made with those carriers but does not include that handled in trains operated by the Salt Lake.

Of the total freight revenues of the Salt Lake in 1936, approximately 61 percent was from the traffic in bituminous coal. Other important items were crude oil, gasoline, and cement. The coal originates at several local stations and is hauled principally to Denver. Mines are numerous in the territory served. The number of carloads handled in 1936 exceeded that of any previous year. The same is practically true of the oil and gasoline. The latter originates at Craig and is shipped to Denver, and to points west

via the cut-off. The Salt Lake's total carload traffic decreased from 32,014 cars in 1929 to 15,801 cars in 1933, then increased each year to a total of 35,213 cars in 1936. The number of carloads delivered to connecting carriers in 1936 was 24,207, and the number received from such carriers was 1,288.

The opening of the Moffat Tunnel in 1928 was followed by a marked increase in the earnings of the Salt Lake, and a further increase followed the opening of the cut-off route on June 15, 1934, owing to the rentals paid to the Salt Lake by the Denver. The latter's net railway operating revenues, however, were reduced. Considering the operation of all lines involved, the net loss due to the cut-off, for the 12 months ended June 30, 1935, was computed at approximately $218,000 on the waybill method of allocating revenues adopted by the debtor, allowing a constructive mileage to the cut-off, or at approximately $285,000 on the waybill basis, allowing the cut-off its actual mileage. The methods used for allocating revenues will be explained in connection with the plans filed.

The Denver's total operating revenues were at a maximum of $34,828,669 in 1929, declined to less than half that amount in 1933, and increased to $25,599,309 in 1936 and $8,180,745 during the first four months of 1937. Net railway operating income, however, did not change proportionately, having amounted to $8,528,676 in 1929, $3,357,643 in 1933, and $1,569,814 in 1936. This decline may be ascribed to the steady increase in operating expenses, taxes, and joint-facility rents. The emergency freight surcharges collected in 1932 and 1933, under the authority of the Commission in Ex Parte No. 103, amounted to $380,862, and during 1935 and 1936, under Ex Parte No. 115, to $547,457. Wage reductions made under agreements with organized labor amounted to $851,780 in 1932, $876,876 in 1933, $872,996 in 1934, and $118,024 in 1935. Wages were fully restored on April 1, 1935. The estimated amount of the charges to tax accruals in 1936 on account of the Federal Railroad Retirement Act was $403,479 and on account of the Social Security Act, $135,017.

The Denver reported a nonoperating income of $675,615 in 1935 and $709,590 in 1936. An analysis of the first figure shows the principal subitems to be income from lease of road and equipment $245,241, dividends on the stock of the Salt Lake Western $145,240, and interest on a bearer note of the Salt Lake Western $128,372. After intercompany eliminations, the nonoperating income (including $66,320 as that of the Salt Lake in the same year) amounted to $223,081. Miscellaneous deductions from income aggregated $260,828 in 1935 and $258,547 in 1936. Income of the

Denver available for the payment of interest was $8,938,657 in 1929, $3,497,991 in 1933, and $2,020,857 in 1936. The net income in 1929 was $3,554,110, and the income deficits in 1933 and 1936 were $2,139,757 and $3,911,204, respectively.

The operation of the narrow-gage lines is reflected in the foregoing figures. About 88 percent of the net ton-miles of these lines is within the territory subject to the lien of the D. & R. G. first consolidated mortgage. The system revenues contributed by the traffic handled from and to points on these lines aggregated $1,953,000 in 1934 and $2,017,000 in 1935. The debtor considers that the system revenue derived from the freight traffic originated on the narrow-gage lines about equals the operating loss on such lines.

During each year of the three years ended June 30, 1935, the income of the Denver available for the payment of interest represented approximately 1.12 percent of the average book investment in road and equipment, less accrued depreciation on equipment.

The total railway operating revenues of the Salt Lake declined from the high level of $3,981,131 in 1929 to the low of $1,620,006 in 1934, increasing to $2,234,882 in 1935, and to $2,856,949 in 1936. The corresponding net revenues from railway operations for 1929, 1934, and 1936, were $1,754,484, $805,155, and $918,281, and the net railway operating income $1,679,287, $913,122, and $1,090,810. The emergency freight surcharges on the Salt Lake amounted to a total of $119,121 during the years 1932, 1933, 1935, and 1936. The wage reductions aggregated $50,863, the charges under the Railroad Retirement Act $50,037, and those under the Social Security Act $17,542. The Salt Lake reported net income of $610,069 in 1929, $12,493 in 1934, and $2,455 in 1936.

The combined income accounts of the Denver and the Salt Lake for the years 1927 to 1936, inclusive, with adjustments for intercompany charges and credits, and for an error appearing in the account for 1935, show a downward trend in the income available for interest from 1929 to 1932, a fairly constant level between 1932 and 1935, when it averaged about $3,600,000 a year, and $2,417,746 available in 1936.

The reports of the Bureau of Accounts, filed in this proceeding by order of division 4, show the result of corrections in the carriers' income accounts, 1930 to 1934, inclusive, for accounting not in accordance with our regulations, an adjustment to include income items entered in profit-and-loss account by our permission and a further adjustment to give retroactive effect to the excise tax in connection with the Railroad Retirement Act, effective March 1, 1936, the Social Security Act, effective January 1, 1936, and our order respecting accounting for equipment depreciation, effective

January 1, 1935. The combined effect of these changes is to reduce the average income of the Denver available for the payment of interest from $4,243,563 per annum to $3,521,239 per annum during the period. On the same basis the average available income of the Salt Lake is reduced from $655,771 per annum to $540,395 per annum.

Although the combined total revenues of 1936 were substantially in excess of those of 1935, the net revenues were less largely because of the heavy maintenance program. Maintenance-of-way expenditures for the system increased from $2,752,695 in 1935 to $4,453,359 in 1936; and maintenance-of-equipment expenditures increased from $5,285,329 in 1935 to $7,215,066 in 1936, notwithstanding the abnormally high maintenance expenditures in 1935 as reflected in the adjustments made by the debtor in the earnings for the year ended June 30, 1935, hereinafter discussed.

On the Denver in 1936 operating expenses were charged with $836,614 in connection with capital charges of $1,314,392 for roadway. On the Salt Lake the operating expenses were $248,005 in connection with $668,574 of capital charges.

In 1936 the Denver expended approximately $1,200,000 on maintenance-of-way work deferred from prior years and in connection with improvements. For maintenance of equipment $800,000 was spent under like requirements. The Denver proposed an improvement program for the years 1937, 1938, and 1939, involving a total capital expenditure of $6,179,700 for road and equipment, with operating charges of $4,070,800, and cash requirements of $9,905,200 in connection with such improvements.

The Salt Lake's line has been largely rebuilt during recent years and the amount of deferred maintenance is evidently slight. A witness for the Finance Corporation considers the line to be virtually a new railroad. However, an improvement program for the years 1937, 1938, and 1939 was contemplated by a director of the Salt Lake, under which the expenditures would be $2,194,000 for road and equipment and $693,000 for operating expenses. More than half this outlay would be made for reducing curvature and revising the alinement. The debtor's testimony was to the effect that the expenditures for improvements would have to be continued for two or three years longer in order to bring the Salt Lake up to the standard of the Denver. Incidental to the showing made by the Finance Corporation with respect to the Salt Lake, a study was introduced in which the income available for interest was estimated at $1,449,000 for 1936 on the basis of the Salt Lake's operation as an independent carrier, assuming no further rehabilitation of the line between Orestod and Denver to be necessary.

A study for a determination of the earnings of the Denver and the Salt Lake during a normal year was presented by the president of the Denver, such study indicating that the total railway operating revenues of both roads would be $33,721,189, the total railway operating expenses $23,918,282 (operating ratio 71.49 percent), the net railway operating revenue $6,435,857, and the income available for interest, $6,215,423. In the opinion of the witnesses such results were to be expected in 1939. The debtor's estimate of freight traffic, which was made in collaboration with the officers of two trunk lines that connect with the Denver, was based on a study of the traffic in each principal commodity handled between 1928 and 1936, and the number of carloads, average tonnage, and average revenue per car for a normal year were estimated in the case of each commodity. Consideration was given to business conditions in the local territory and to the trend of production, to the effect of opening the cut-off, and to present and prospective rate levels. A substantial increase in the traffic connected with the mining industry is reflected in the forecast. Operating expenses were based on the total amount of revenues estimated. A continuation of the present scale of wages was assumed. Maintenance expenses for the Denver were fixed at 33 percent of gross revenues, which compares with an average of 35 percent for the years 1925 to 1936 inclusive. For the Salt Lake the ratio was taken at 30.7 percent.

A study of the prospective revenues of the combined lines was also made by a bank officer, testifying as a financial expert in the debtor's interest, who showed that the operating revenues of the Denver since 1933 represented an increasingly large proportion of the operating revenues of all class I roads. By relating the trend of railroad earnings to the number of workers employed in the durable-goods industries, and making certain assumptions as to normal conditions in industry and in railroad rates, the witness arrived at an estimate of $32,559,560 for the total operating revenues of the Denver. Such sum is $1,825,560 in excess of the "normal" revenues shown in the president's forecast.

The debtor selected the 12 months ended June 30, 1935, as the basis for the allocation of earnings to mortgage districts in connection with the development of its plan of reorganization. In this so-called test period, the total railway operating revenues of the system were $21,828,298, the total railway operating expenses $16,485,571, the net railway operating income $3,149,965 and the income available for interest $2,923,024.

These figures were materially changed, as will be shown in describing the debtor's plan, by adjustments made in order to elim-

inate abnormalities in operating conditions during the test period and to establish a level of earnings which would be generally representative, giving effect to the opening of the cut-off route. Thus the income of the Denver assumed as available for interest was increased from $2,084,783 to $2,813,063, and by adding the earnings of the Salt Lake's independent operation, together with the estimated savings under unified operation, the system income available for interest based on the test-period year was placed at $3,926,223. This was the figure used in computing the amounts of new bonds assignable to the present first-lien bondholders on the basis of the respective earnings of different divisions of the system, but in the determination of the amount of future fixed charges permissible still another change of base was introduced viz, the average earnings of 1932, 1933, and 1934. With certain adjustments, this computation indicated $3,687,328 as the income of the system available for the payment of interest.

Debtor's Plan of Reorganization

The debtor's plan, dated July 28, 1936, is based upon a consolidation of the properties of the Denver, the Salt Lake, the Salt Lake Western, the Junction, and the Goshen Valley. The amount, character and distribution of securities to be issued by the new company were determined primarily from earnings. During the course of the hearing the debtor at the request of certain interveners, made additional studies of the earnings of the lines subject to first-lien mortgages, arriving at a distribution of the new securities which differed materially from that originally proposed. On brief, the revised distribution is favored, yet the debtor states that it does not desire technically to amend the original plan.

In order to ascertain the earnings of the several mortgage districts as a basis for the apportionment of new bonds, the debtor adopted a formula or general method, which was applied to the revenues and expenses of the Denver for the 12 months ended June 30, 1935. The Salt Lake was not included in the first step of the analysis, since its mortgages apply to the entire line and its earnings are separate from those of the Denver. Freight revenues of the Denver were divided among the mortgage districts on an average ton-mile basis, and it was considered proper to assign the same mileage to the cut-off route between Denver and Dotsero as that of the old route between those points via Pueblo, although the latter route is approximately 175 miles longer.

It appears from the revised figures, as has been stated, that the operation of the cut-off during the first year resulted in a system loss of approximately $218,000, because of increased transporta-

tion costs despite a substantial increase in through traffic. The effect of the diversion of traffic to this route was to deprive the lines subject to the lien of the D. & R. G. first consolidated bonds of approximately $900,000 of annual revenue, which would otherwise have accrued to such lines if the same traffic had been handled.

Maintenance-of-way expenses were adjusted in a manner intended to show normal conditions over an average period. For the cut-off, much larger expenses than the actual were used. Maintenance-of-equipment expenses were apportioned to engine districts on the basis of equipment mileage, using the years 1933 and 1934 as typical, and certain assumed ratios were employed in dividing the total expenses of locomotive repairs between the freight and passenger services.

For the use of equipment, the charges to each first-lien mortgage were made on the basis of 2 percent per annum applied to the ledger value of the equipment used, less depreciation. The mortgage with a lien on the most equipment represented the district where the smallest use of equipment took place. The use of the 2-percent rate will be referred to later. Yard switching expenses were distributed on a car-mile basis over the different divisions of the system. This method was also followed for maintenance expenses of yards and yard locomotives, station services, and so forth.

The adjustments made in the actual earnings of the Denver during the test-period year consisted principally of a reduction of approximately $714,000 in total maintenance charges, a reduction of $452,618 in nonoperating income, due to intercompany eliminations, of which reduction $65,889 was not specifically explained, and the elimination of $261,570 of miscellaneous deductions from income, of which $10,807 was not explained. To the income of the Denver there were added $182,342 to compensate for the abnormally low earnings from the potato traffic originating in the San Luis Valley, and $83,333 to represent the earnings of the Utah Fuel Company. As a result of all adjustments the income of the Denver available for interest was finally shown as $2,813,063, and the corresponding amount for the consolidated system as $3,926,223.

Objections to the use of the year ended June 30, 1935, as an earnings base were expressed by the trustee of the R. G. Western consolidated mortgage, the trustee of the Denver's refunding and improvement mortgage, the Untermyer family group, and the Security Research Bureau. In general, these interveners urged that the base should reflect conditions after the cut-off route shall have become definitely established.

The entire formula is admittedly open to objection and is largely a matter of judgment. Controversy arose especially in regard to the debtor's treatment of the cut-off, the priority of mortgage liens with respect to equipment, the rental charged for equipment, the segregation of company freight, the allocation of branch-line losses, the adjustment for the higher rate scale on the narrow-gage lines, and the period chosen as representative of earning power.

The debtor revised its first formula in various respects, principally by allocating freight revenues according to actual waybills to the extent records thereof were available, by segregating company freight and including only so much of the cost of handling as was involved where one mortgage district bore the expense of work done by another, by separating train switching from general road operation and by charging the narrow-gage districts with the cost of transferring freight from narrow-gage to standard-gage cars, and vice versa. The test-period basis of earnings, as adjusted, was retained, but the revisions just mentioned resulted in substantial changes in the allocations.

A further revision of the formula showed the effect of computing the earnings of the cut-off operation on a straight mileage basis. This analysis was utilized in part by the committee in preparing its plan, as will be explained.

From the primary distribution of earnings, the ratio of the earnings of each mortgage district to the total was established. These ratios were next applied to the total fixed interest charges considered permissible for the new company. In the detailed computations such charges were taken at $2,598,474, and in the final set-up for the new capital structure they are shown as $2,584,165. The debtor offers further support for the proposed total fixed charges by referring to the average income available for interest during the 3-year period 1932–34, which with certain adjustments was $3,687,328, or 1.42 times the amount of the charges adopted.

After the distribution to each mortgage district of its proportionate share of the proposed new interest charges, such shares were compared with the earning power of each district, as established on the basis of the test-period performance. In the case of certain districts, such as those represented by the Junction first mortgage and the R. G. Western first-trust mortgage, the earnings exceeded the proposed fixed interest charges; in other divisions deficiencies were shown. The surpluses were passed on to the next junior obligations, and were considered in fixing the amount of new bonds to be offered to the present bondholders, the Finance Corporation, and the Credit Corporation. The Finance Corporation, by virtue of its lien on the stocks of the Salt Lake and Salt

Lake Western, was credited with the earnings of the cut-off route and those of the Salt Lake's separate operation. It was also credited with the dividends paid on the stocks of the motor carriers. From calculations based on the revised formula, the debtor arrived at new proportions for the distribution of first and refunding mortgage bonds, general-mortgage bonds, and first preferred stock to the holders of the present securities. The record of market prices of the debtor's securities was given some weight in determining the allocation of new securities.

The debtor proposes to leave the equipment obligations undisturbed to call in the Salt Lake's bonds for redemption, to issue bonds under three new mortgages, and to issue three classes of new capital stock, all to be exchanged for existing bonds, stocks, and the notes to the Finance Corporation and Credit Corporation in varying ratios. A new collateral note would be issued to the Chase National Bank. No provision is made in the plan for the trustee's certificates outstanding, which, according to the debtor's principal witness, will be paid at maturity. The Western Pacific and the Missouri Pacific would retain stock control of the new company, but each would relinquish the $1,000,000 of refunding and improvement mortgage bonds which it owns, and in addition each would agree to purchase $1,500,000 of new bonds at par. In connection with the equity in the present common stock, the debtor showed that between 1925 and 1935 approximately $4,383,000 was expended for improvements from net income which might have been applied to dividends on the common stock. A statement of the cost of the improvements made on each mortgage district and on the Salt Lake was supplied for the record.

Under this plan new income bonds are to be offered for the 460 shares of Salt Lake stock outstanding in the hands of the public. The Finance Corporation was expected to underwrite $11,443,680 of new first and refunding mortgage bonds, and to accept $11,317,950 of such bonds as payment of the debt to it.

Accruals of unpaid interest on the present bonds and short-term debt of the Denver, excluding pledged bonds, amounted to $14,293,464 as of December 31, 1936. The debtor makes no provision for interest not earned during the trusteeship, amounting to approximately $4,770,000. Other accrued interest is to be funded in new securities junior in rank to those issued against the principal obligation.

The new capitalization proposed by the debtor, based on the obligations actually outstanding on December 31, 1936, would be as follows: Equipment-trust obligations, $1,805,000; Western Division 3½-percent bonds, representing a first lien on the stand-

bonds, as provided in the plan for the purpose of refunding the first-mortgage and income bonds of the Salt Lake now outstanding.

The new capitalization proposed by the committee, based on the obligations actually outstanding on December 31, 1936, would be as follows: Equipment-trust obligations $1,805,000; first-mortgage bonds, series A, $18,563,533; series B, $52,057,197; income-mortgage bonds, $27,042,895; a collateral note for approximately $1,593,948; preferred stock, $26,403,389, par value; common stock, of no-par value, class A, 349,002 shares; warrants for class-A common stock, 164,456 shares; and warrants for class-B common stock, 200,000 shares; total capitalization approximately $128,179,000, taking the no-par common stock at $1 a share. The above total of first-mortgage bonds includes $6,000,000 of bonds proposed to be issuable to redeem trustee's certificates, to provide for reorganization expenses or working capital, or to be applied to other approved purposes. Securities to be issued and pledged are not included in the above summary. Approximately $58,000 in cash would be paid to the holders of certain divisional bonds as an adjustment of interest rates.

The committee argues that the above-mentioned $6,000,000 of first-mortgage bonds should not be included in the proposed capitalization or fixed interest charges, on the theory that cash would be available to retire the trustees' certificates or the bonds issued against them, or in any event the improvements recently made would result in operating economies more than adequate to pay the $240,000 of annual interest on the additional $6,000,000 of new bonds. We think, however, that in any comparison of plans this block of bonds and the interest thereon should be included. In doing this an interest rate of 4 percent will be applied.

On this basis, under the committee's plan, the total amount of fixed-interest debt (omitting the amount due the Railroad Credit Corporation) would be approximately $74,020,000 and the annual fixed interest charges $2,957,000. Contingent interest charges would be approximately $1,217,000 per annum and the dividend requirements on the preferred stock $1,320,000 per annum, not including pledged securities.

The foregoing charges do not include payments to a capital fund up to 2½ percent of total railway revenues, subject to a maximum of $750,000 a year, which is made mandatory under the committee's plan. The committee devoted all of its estimated $2,774,554 of income available for fixed charges to the issue of new first-mortgage bonds, series A and series B. It then computed the allowable amount of contingent-interest bonds from earnings of

about $4,000,000, considered applicable to fixed and contingent interest charges, again disregarding the payment to the capital fund, which, however, is placed before contingent interest.

The theoretical application of income available for interest annually under the committee's proposal would be in the following sequence: (1) Fixed interest; (2) fund for additions and betterments ($750,000); (3) contingent interest; (4) sinking fund for the income bonds ($67,607); and (5) dividends on preferred stock; grand total, before dividends on the common stock, $6,312,000.

Under this plan, the Junction first-mortgage bonds and the R. G. Western first trusts would receive new first-mortgage bonds in amounts equal to the principal of the present bonds, respectively, plus accrued interest. In the case of all other bonds, various proportions of first-mortgage series-B bonds, income bonds, and preferred stock are assigned, except that class-A common stock, only, is to be issued for the present general-mortgage bonds, and the present bonds of the Salt Lake are to be called for redemption and paid through the issue and sale of new first-mortgage series-B bonds, as has been noted. Income bonds in the amount of $9,931 are proposed to be issued to the holders of the 460 shares of Salt Lake outstanding in the hands of the public. The new class-A common stock, allocated to the holders of general-mortgage bonds is to be placed in a voting trust pending the disposal of the matter of equity in the present common stock, as hereinafter explained.

The holders of the 164,450 shares of preferred stock would be offered warrants for the purchase of a like number of shares of new class-A common at a suggested price of $20 a share. The holders of the 300,000 shares of common stock would be offered, pro rata, warrants for 200,000 voting-trust certificates or shares of new class-B common stock at $30 a share, at any time within 6 months from the date of effectuation of the plan. In the event this option is not exercised, an assignable option, in the form of warrants, would revert to the reorganization committee for the purchase of 200,000 shares of class-B common at $30 a share, within 3 years from the effectuation of the plan. The reorganization committee would be authorized to transfer such option to any interests that it may select as being of the greatest advantage to the new company. The committee suggests the advisability of offering part of the option to the Chicago, Burlington & Quincy Railroad Company and the Chicago, Rock Island & Pacific Railway Company, because of the importance of these connections at Denver, and it is contended that there should be no objection to this association of interests on the part of the Missouri Pacific. Representatives

that the provision of section 77 (b) (5), permitting a sale at not less than a fair upset price, was designed for the identical purpose here in view.

The committee's plan, as well as the debtor's plan, is unacceptable to the trustee of the refunding and improvement mortgage, who undertakes to show that the rights of the bondholders are not adequately recognized under either plan. The trustee of the D. & R. G. first consolidated mortgage prefers the committee's plan but complains of the diversion of traffic and earnings to the cut-off route reflected in the results. The successor trustee under the R. G. Western first consolidated mortgage prefers the committee's plan but contends that the holders of bonds issued under this mortgage are entitled to better treatment than is offered under either plan. The Untermyer family group, owners of D. & R. G. first consolidated mortgage bonds, refunding and improvement mortgage bonds, general-mortgage bonds, and preferred stock of the Denver, contend that both plans are unfair to the present security holders in many respects and should be disregarded by us in formulating a new plan. The Security Research Bureau recommends several modifications in the committee's plan.

The trustee under the debtor's general mortgage prefers the committee's plan to the debtor's but on brief contended that the committee treated the general-mortgage bonds inequitably in relation to the unsecured creditors and the stockholders, and that a new class of second-preferred stock should be allocated to the general-mortgage bonds in place of the class-A common stock provided in the committee's plan. Later, in connection with its exceptions to the examiner's proposed report, the trustee suggested that the committee's plan be revised by eliminating the provisions for new common stock of classes A and B, and substituting a single class of no-par common stock, of which 750,000 shares would be issued in the reorganization. Of such stock, 408,618 shares would be issued to the holders of the general-mortgage bonds in satisfaction of their total claims for principal and interest ($44,587,800, including the interest from February 1, 1924, to February 1, 1929), 4,400 shares would be issued to the unsecured creditors, and 314,350 shares would be reserved for conversion of the new preferred stock. The 413,018 shares would be placed in escrow for a period not exceeding 5 years, and rights for the purchase of the stock at $100 a share would be issued to the debtor, or to the stockholders individually if an agreement could be reached between the two classes of present stock as to the proper allocation between them of such rights. The proceeds of sale would be distributed pro rata to the holders of the certificates of deposit, i. e., the present

holders of the general-mortgage bonds. This proposal is urged as a means of satisfying the claims of these bondholders before recognizing the stockholders, and at the same time avoiding a determination of the question of the equity represented by the stock. Apparently, if fully carried out, the plan would mean the payment by the proprietary companies of $41,301,800 in cash for control of the new company. It would further mean that the holders of the general-mortgage bonds would receive substantially the full amount of their claim in cash, while senior bondholders would be asked to accept various amounts of new securities, in some cases only income bonds and preferred stock. The largest single holder of the general-mortgage bonds is the Western Pacific Railroad Corporation, which is not represented in this proceeding.

In connection with the general-mortgage bonds, the trustee insists that any plan of reorganization should recognize the claim for interest, in the amount of $7,452,000, accrued between February 1, 1924, and February 1, 1929, in addition to the $7,327,800 of interest accrued between February 1, 1929, and June 30, 1938, the latter clearly being fixed interest under the provisions of section 4 of article 6 of the mortgage. The same section provides that the payment of interest accrued prior to February 1, 1929, shall not be mandatory even if earned, but if earned and available it shall be paid to the extent that, in the reasonable discretion of the board of directors, such payment is not inconsistent with due regard for the protection of the property and the maintenance of efficient service. Section 2 of article 8 provides that no dividends on any class of stock may be paid unless and until the full cumulative sinking-fund payments and the full cumulative interest on the general-mortgage bonds shall have been declared and paid, or set apart for payment.

In preparing its plan the debtor evidently considered the payment of interest prior to February 1, 1929, as discretionary and not a fixed charge. Counsel, on oral argument, offered no definite opinion on this point. The committee's plan does not include this interest as part of the obligation to the general-mortgage bondholders. Our view of the matter is that the claim of these bondholders is so large in relation to the indicated equity remaining for them, that as a practical matter it is immaterial whether the interest in dispute is included or not. For the purpose of the plan we shall therefore exclude this interest from the claim, without prejudice, however, to a judicial determination of the matter.

Because of the usual seasonal traffic fluctuations, the use of 6-month income periods for the determination of available net income, and the payment of interest and preferred-stock dividends

semiannually, as proposed by the committee, involves successive adjustments of bond interest and the use of interim dividends on the preferred stock in order that the aggregate payments to the security holders shall be based on the earnings of complete calendar years. This method, it is true, would result in a return to the security holders twice a year, earnings permitting, but it is desirable that the result of a full year's operation be ascertained before any contingent interest or dividends be paid (subject to the condition that the initial income period is six months), and that the entire amount of such interest and dividends earned be paid as soon after the close of the 1-year income period as is practicable. The date of the payment should be as stated below.

As has been shown, the debtor's proposal for a capital fund was that an annual payment of $350,000 be made from available net income after the payment of fixed charges, and that a second payment, representing the difference between $350,000 and 3 percent of total revenues, be made after the payment of interest on the proposed income bonds, if earned. The debtor's principal witness considered that 3 percent of total revenues would be a fair amount to be set aside for the capital fund, considering the amount of expenditures in the past and the possible difficulty of new financing at times in the future. As the committee views the matter, payments into the fund should be made semiannually in amounts up to 2½ percent of total revenues, subject to a maximum limit of $375,000, or $750,000 on an annual basis, the entire payment to follow directly the payment of fixed charges. We approve the latter provision on the ground that, if there is to be a mandatory capital fund; all payments thereto should precede the payment of contingent interest, and we further approve a limitation on the amount to be paid into the fund each year. The average gross charge to investment in road and equipment for the system lines during the 10-year period 1926–35 was $3,273,668 per annum, which is far in excess of 3 percent of the average annual gross revenues during that period. From the evidence it is difficult to predict the yearly capital requirements of the system after the present rehabilitation programs shall have been carried out, and obviously impossible to foretell future financing conditions. Following the debtor's plan, 3 percent of the average annual revenues during the 10-year period 1927–1936 would have been $848,203. On the basis of the estimate for a future normal year, 3 percent of the revenues would be $1,011,636. The principal witness for the Finance Corporation approved the committee's proposal for a maximum payment of $750,000, considering it sufficient.

Conclusions

The consolidation of the several companies for unified operation and management, which is an essential part of the plans that have been presented, is in accord with our findings in *Consolidation of Railroads*, 159 I. C. C. 522, wherein the Denver and the Salt Lake were grouped in system No. 18, Missouri Pacific. The Western Pacific was also included in that system, but the present record is inadequate for a determination of the question of merging the Western Pacific with the reorganized Denver. It justifies the conclusion, however, that the consolidation of the Denver, the Salt Lake Western, the Salt Lake, the Junction, and the Goshen Valley would be in the public interest, as unifying the Denver and its subsidiaries, eliminating unnecessary separate corporations, and effecting operating economies. Notwithstanding the fact that the Salt Lake, the Junction, and the Goshen Valley are not in trusteeship, and that none of the corporations has sought consolidation under section 5 (4) of the Interstate Commerce Act, as amended, we conclude that a consolidation of the aforesaid properties should be effected in connection with the plan. Any corporate action by the existing companies which may be necessary under the requirements of section 5 (4) of the Interstate Commerce Act, as amended, will be assured if and when our plan shall have been accepted in the manner provided in section 77 (e). As pledgee of the capital stock of the Salt Lake, the Salt Lake Western, and the Goshen Valley, the Finance Corporation is at present in a position of control with respect to the action of those corporations. The Governors of the States in which the several carriers operate were served, prior to the hearing, with copies of the plan of reorganization filed by the debtor, and advised of the provisions for consolidation contained therein.

The Public Service Commission of Utah, on its own behalf and on that of the Uintah Basin Railroad League, opposes the absorption of the Salt Lake in the new system on the ground that the independence of that carrier would facilitate the building of an extension westward from Craig through the Uintah Basin to Provo or Salt Lake City. These Utah interests likewise opposed the acquisition of control of the Salt Lake by the Denver. Such acquisition having been authorized by us and carried out, we think that this reorganization should not be hampered by the position taken by the Utah Commission. In view of the Denver's control of the Salt Lake, a consolidation of the roads will not alter the present situation in such a way as to prejudice the construction of a line through the Uintah Basin.

ard-gage lines west of Dotsero, $22,680,233; first and refunding mortgage 4-percent bonds, representing a first lien on all standard-gage lines east of Dotsero and a second lien on all other standard-gage property, $48,222,730;[1] general income mortgage 4-percent bonds cumulative for two years, representing a lien junior to that of the first and refunding bonds, $18,686,850; first preferred 4½-percent noncumulative stock, of $100 par value, $30,376,050; participating preferred 5-percent stock, of no-par value, 413,842 shares; common stock, of $1 par value, 200,000 shares; and a collateral note for $1,542,200 issued to the Chase National Bank. The bonds and stock proposed to be pledged as security for this note are not included in the foregoing totals.

The amount of first and refunding bonds stated includes $6,000,000 of bonds to be placed in the treasury of the new company to provide funds for 100 percent of the cost of additions and betterments and other corporate purposes during the first year after reorganization, of which bonds $3,000,000 would be available for immediate sale to the public and $3,000,000 would be available for sale to the Missouri Pacific and Western Pacific as required. Approximately $277,000 in cash would be paid to the holders of certain divisional bonds as an adjustment of interest rates. The debtor considers that the minimum amount needed for cash working capital is approximately $1,000,000. The provision for treasury bonds to be available for sale is considered by the debtor preferable to providing any specified amount of cash in the reorganization for working capital and additions and betterments.

The capital stock of the Utah Fuel Company would be pledged under the proposed general mortgage. As has been indicated, this stock is now under the first lien of the R. G. Western consolidated mortgage, subject to a right of redemption upon the payment of $6,000,000 in cash or upon the deposit with the mortgage trustee of $6,000,000, principal amount, of the consolidated-mortgage bonds. The company's balance sheet of December 31, 1936, shows the asset value of the fuel company property as $15,171,943, the par value of stock outstanding as $10,000,000, and the corporate surplus as $2,652,839. An appraisal of the property, made for the trustee of the R. G. Western consolidated mortgage by a mining expert, indicated a going-concern value of $4,653,720. As has been stated, the debtor, in applying its formula for allocation of earn-

[1] Not including additional future issues for (1) the purpose of refunding the $2,217,000 first-mortgage bonds of the Northwestern Terminal Railroad Company in the event that it is desired to utilize permanently the facilities of that company, (2) exchange for securities of the Western Pacific Railroad Company in the event of a consolidation with that company, and (3) refunding the Western Division bonds which may be issued.

ings by mortgage districts, credited this mortgage with an income of $83,333 per annum from the fuel company, based on dividends paid but not earned in the period 1932–34. In 1935 and 1936 small amounts of net income were reported. The property and its operations are completely described in the record. As part of the security for the R. G. Western consolidated-mortgage bonds, its value is an element in the claims of the trustee under that mortgage.

Including $1,805,000 of equipment obligations and $650,000 of trustees certificates, the total funded debt of the new company under the debtor's plan would be $92,937,013, the fixed interest charges $2,868,235, per annum, and the contingent interest charges $747,474 per annum. Dividend requirements on the first preferred stock would be $1,366,922 and on the participating preferred $2,069,210 per annum. The total capitalization of the new company, if a par value of $1 a share be assigned to the participating preferred stock, would be $123,926,905.

The theoretical application of income available for interest annually would be in the following sequence, under the debtor's program immediately upon consummation of the plan; (1) Fixed interest, $2,868,235; (2) fund for additions and betterments, $350,000; (3) fund for retiring first and refunding bonds (one-half of 1 percent per annum on the maximum principal amount at any previous time outstanding), $241,113; (4) contingent interest on income bonds, $747,474; (5) second payment to the fund for additions and betterments, 3 percent of gross revenues less $350,000; (6) fund for retiring income-mortgage bonds (one-fourth of 1 percent on the maximum principal amount at any previous time outstanding), $46,717; (7) dividends on the first preferred stock, $1,366,922; (8) dividends on the participating preferred stock, $2,069,210; grand total before dividends on the common stock, $7,939,671.

The foregoing figures omit provision for the payment of any undistributed-profits tax under the Revenue Act of 1936. The debtor submitted an estimate of the amount of such tax in the future, based on various amounts of net income available for interest, indicating $180,000 per annum as a probable maximum.

Expenditures for additions and betterments during three years after reorganization would be initially capitalized in full through the issue of not exceeding $6,000,000 of first and refunding mortgage bonds to be issued as treasury bonds. Thereafter, bonds might be issued under either the western-division mortgage or the first and refunding mortgage up to 75 percent of the cost of additions and betterments, the remaining 25 percent to be supplied through the proposed capital fund. The debtor's intention is that

the new first and refunding mortgage bonds shall constitute the principal medium, but not the only medium, of future financing.

As has been stated, the holders of unsecured claims, not coming under the six-months rule and not paid off currently, would receive new participating preferred stock at the rate of one share for each $100 of claims. This is with the proviso that, should any general creditors prove to have claims secured to such an extent as to justify better treatment, the debtor company, as reorganization manager, should be authorized to allocate other securities in settlement of such claims, subject to our approval. The debtor is of the view that the treatment of executory contracts, including the Northwestern Terminal Railroad Company lease, should be left to the new management and the court.

The plan is the result of a comprehensive study by the secretary-treasurer of the Missouri Pacific, and was made at the request of representatives of that company and the Western Pacific, acting as a managing committee of the Denver. Conferences on the development of the plan were held by its proponents with representatives of the Finance Corporation, the Chase National Bank, the Insurance Group Committee, and others. Resolutions approving the plan were enacted by the boards of directors of the several companies involved, except the Salt Lake and the Goshen Valley; but no action has been taken with respect to the application for authority to consolidate the properties in accordance with section 5 (4) of the Interstate Commerce Act, as amended. The debtor contends that under the provisions of section 77 (b) applications for authority to consolidate are unnecessary.

Disapproval of the debtor's plan was expressed by the Insurance Group, the Security Research Bureau, several mortgage trustees, the Railroad Credit Corporation, the Finance Corporation, and others. The Finance Corporation declined to give its consent, as pledgee of the stocks of the Salt Lake and the Goshen Valley, to the concurrence of these companies in the plan. It contends that during the period of the Denver's trusteeship no rental has been paid for the use of the Salt Lake Western line, nor have the trustees acted either to affirm or disaffirm the lease.

The chairman of the Finance Corporation is in favor of a consolidation of the Western Pacific and the Denver. A special committee of the latter's directors was appointed to negotiate such a consolidation, and in the event that it was undertaken the debtor was to file a supplemental plan. The debtor considers that the proposed western division mortgage might be extended to cover the Western Pacific property, and certain of the bonds reserved

under that mortgage could be issued to the holders of Western Pacific securities.

The Finance Corporation introduced evidence pertaining to the cut-off route, as compared with the route via Pueblo, for the purpose of showing the superiority of the former in respect of grades, curves, and other physical features, cost of moving freight and passengers, originated traffic, and many other matters. It contends that its loans to the Denver are fully secured, that it has extensive powers of control over the Salt Lake and the Salt Lake Western, and that it is entitled to such treatment in the reorganization as will fully satisfy its claims. Objection was made to the debtor's proposed offer of new bonds which would represent only a second lien on the western lines, and it was urged that all unpaid interest should be paid in full.

Insurance Group Plan

The Insurance Group committee represents seven mutual life-insurance companies which, taken together, owned $15,874,000 of bonds issued under the Denver's underlying mortgages, principally the R. G. Western and D. & R. G. first consolidated, but no bonds issued under the debtor's own mortgages. The holdings represent more than 10 percent of the principal amount of the bonds in each class outstanding. These insurance companies owned more than $91,000,000 of bonds and equipment obligations of the Missouri Pacific and its subsidiary companies, and nearly $15,000,000 of similar securities of the Western Pacific.

The formula used by the committee for the distribution of revenues and expenses is a modification of the debtor's formula, based on the same test period. Consolidation of the properties is likewise contemplated and, while consolidation with the Western Pacific is not directly provided for, the committee states that its plan leaves the way open for such consolidation.

The committee used the debtor's distribution of earnings by mortgage districts, as revised on the basis of actual waybills, adjusting the results thereof (1) by allowing 42 percent of the constructive-mileage adjustment for the cut-off, (2) by reallocating a certain group of equipment, and (3) by recognizing all fixed interest charges unpaid up to December 31, 1936. The net result of the changes was to increase the amounts of test-period earnings (totaling $3,926,223) assigned to the Junction first mortgage, the R. G. Western first-trust mortgage, and the D. & R. G. first consolidated mortgage, and to reduce the amounts assigned to other items, notably the lines subject to the lien of the Finance Corporation notes.

The arbitrary allowed to the cut-off in the committee's plan arises from an adjustment of the debtor's ascertainment of unit operating expenses for the two routes, respectively, such adjustment being confined to maintenance costs, which, it was thought, the debtor had not treated on a comparable basis. Rejecting the debtor's various reasons for the 175-mile arbitrary allowed to the cut-off, the committee asserts that if the cut-off were operated as a separate railroad no division of the through rate could reasonably be expected to exceed the 42-percent allowance.

The committee's adjustment with respect to the allocation of equipment results in a credit of $26,665 to the earnings of the D. & R. G. first consolidated mortgage district and a debit of like amount to the earnings of the refunding and improvement mortgage district. This amount represents the application of the 2-percent rental to equipment having a ledger value, less depreciation, of $1,263,265 as of December 31, 1936, and considered by the committee to be subject to the paramount lien of the D. & R. G. first consolidated mortgage rather than to that of the refunding and improvement mortgage. As to all other equipment the debtor's allocation of equipment under the several mortgages was adopted by the committee. This plan assigns the earnings of the Junction, in excess of the requirements of its present bonds, to the D. & R. G. first consolidated mortgage district, while the debtor assigns them to the refunding and improvement mortgage district.

In applying its formula, the committee arranged the present mortgages in four groups, viz, the R. G. Western district, the D. & R. G. district, the R. & I. district, and the R. E. & C. district, and based its computations on the total earnings allocated to each. In the case of the R. G. Western district, $16,415,667 of new first-mortgage fixed-interest bonds were to be issued for a like amount of claims of the present first-trust bonds, both actually outstanding and pledged, with all unpaid interest to December 31, 1936. This treatment recognizes the fact that the test-period earnings were in excess of the interest requirements of the first-trust bonds. For the total claims of the R. G. Western consolidated-mortgage bonds, the committee proposes to issue $8,938,577 of new first-mortgage bonds and $9,506,025 of new income bonds, the latter figure including $567,448 as an allowance for control of the Utah Fuel Company. The total amount of these new bonds is equal to the total amount of present consolidated-mortgage bonds, with interest. This result is arrived at despite the fact that the earnings in the test-period year, allocated to the consolidated-mortgage bonds, are shown as a deficit of $96,811. It further appears that, although the committee's calculations to determine the allowable

amount of fixed-interest and contingent-interest bonds purport to reflect average earnings during the period 1932–35, the test-period base has been adhered to in fact. In the brief filed by the Security Research Bureau many alleged errors in the calculations are pointed out.

The plan proposes a new first mortgage, secured by a lien on all the consolidated railroad properties, except the narrow-gage lines and their equipment, together with the stock of the Utah Fuel Company. Series-A bonds issued under this mortgage would be convertible into series B, would bear interest at 4 percent, and would mature in 15 years. The reorganization committee would have the power, subject to our approval, to reduce the term to not less than 10 years and to increase the rate of interest to not exceeding 4½ percent, in order that such bonds may be marketable at or near par. The series-B bonds would bear interest at 4 percent and have a term of 40 years. The first-mortgage bonds, which may be limited in amount by the terms of the mortgage, are to be issuable to the extent of 75 percent of the cost of additions and betterments. Income-mortgage bonds, subject only to the lien of the new first mortgage, would be issued under a mortgage closed at the amount of bonds to be issued in the reorganization. The income bonds would have a term of 50 years and an interest rate of 4½ percent, cumulative up to a maximum of 22½ percent. These bonds would be entitled to a sinking fund of one-fourth of 1 percent per annum on the total principal amount of bonds issued in the reorganization.

The plan proposes an issue of convertible preferred stock, entitled to dividends at the rate of 5 percent per annum, cumulative; common stock of two classes; and warrants carrying the right to purchase common stock. A new collateral note would be issued for the present bank debt, and provision is made for the issue of a promissory note to the Railroad Credit Corporation in the event the latter's note is not paid through distributions under the marshaling and distributing plan, or by cash. For the total amount of principal and interest due the Finance Corporation, approximately 58 percent is proposed to be paid in new first-mortgage bonds, series B, and 42 percent in new income bonds.

The chairman of the Finance Corporation advised counsel for the committee that if it is not found feasible to effect a consolidation of the Denver and the Western Pacific, and the plan of the committee is approved by us and affirmed by the court within a reasonable time, the Finance Corporation would finance, at par and accrued interest, $11,443,675 of new first-mortgage 4-percent

of the latter testified as to the established traffic relations between the Missouri Pacific and the Denver, and the possible unfavorable effect of a future alliance between the Denver and other systems, such as the Burlington.

The committee's proposed treatment of the stockholders of the Denver is predicated on a finding that the equity in the present stock is without a value and that the interests of present creditors must receive full consideration before those of the stockholders. However, the committee, recognizing the interdependence of the Denver, the Missouri Pacific, and the Western Pacific, and with a view to maintaining the through route which has been developed, has provided in its plan the above-described means whereby the proprietors may retain control of the Denver.

Cash proceeds received by the new company from the exercise of the warrants are to be used initially to redeem income-mortgage bonds issued to the Finance Corporation. The new class-A common stock would carry full voting power on all matters affecting the essential aspects of its proprietary interests, while the new class-B common stock, if and when one-half of such stock becomes outstanding, would be entitled to elect a majority of the board of directors of the new company, to consist of 12 members. One member would be elected by the holders of the income bonds, two by holders of the preferred stock, and two by the holders of the class-A common stock. The remaining members would be elected by the holders of the class-B common stock.

All the common stock would be issued to the reorganization committee as voting trustees, to be held by them for a period not exceeding 3 years, but the voting trust may be terminated within 90 days from the date of payment for the warrants issuable to the reorganization committee. The reorganization committee would consist of seven members, of whom six would represent a like number of classes of present bonds, and one would be designated by the Finance Corporation.

The plan provides that it shall not be carried out until it shall have been accepted by or on behalf of the holders of at least two-thirds in principal amount of each class of the outstanding bonds of the debtor and by the Finance Corporation, nor unless either (1) the plan shall have been accepted by creditors, other than bondholders and the Finance Corporation, holding at least two-thirds in principal amount of the claims of each class and by the stockholders of each class holding at least two-thirds of the stock of such classes, or (2) provision shall have been made for protecting the interests of such nonassenting classes of creditors and

stockholders as provided in article VIII of the plan, provided that the reorganization committee may under certain conditions eliminate the requirement for consent as to any class of bondholders or the Finance Corporation upon substituting therefor the provision for protecting the interests of the bondholders and the Finance Corporation as is provided in article VIII as to the other classes.

Article VIII of the plan provides for a sale of the debtor's property under certain circumstances in the following manner. If the holders of more than one-third in principal amount of any class of creditors (other than the holders of bonds or the Finance Corporation, except to the extent that the above requirement for a two-thirds consent by the holders of any such class of bonds or the Finance Corporation may have been eliminated by the reorganization committee) of the Denver, the Salt Lake Western, and the Junction, as they have been or may be classified by the court, or the holders of more than one-third of the shares of the Denver's stock of any class, shall not have accepted the plan within such period as the reorganization committee, with the approval of the Commission and the court, may determine, after holders of at least two-thirds in principal amount of each class of bonds affected by the plan and on the part of which two-thirds consent shall be required by the plan as now existing or hereafter modified, shall have accepted the plan, the property of the Denver shall be sold at public auction at not less than a fair upset price as determined by the court, and the nonassenting creditors of such class and/or the nonassenting stockholders of such class, shall be entitled to receive their aliquot proportion of the proceeds of such sale, after deducting therefrom all expenses of such sale and the amount which would be required to pay in full, of principal and unpaid interest accrued to the date of such sale, all creditors whose claims are prior in lien or superior in equity to the claims of such nonassenting creditors or the rights of such nonassenting stockholders. Upon any such sale the property may be purchased for the benefit of the new company by the reorganization committee, and in that event there shall be applied on account of the purchase price therefor the distributive share of the proceeds of sale of all securities the holders of which shall have assented to the plan and the securities, though not assenting to the plan, of all classes of which two-thirds or more in amount have assented to the plan.

This provision was incorporated because of doubt whether the confirmation of the plan, without acceptance by two-thirds in amount of each class of creditors and stockholders, would be within the scope of the bankruptcy power or would be permissible under the due process clause of the Constitution. Counsel assert

New capital structure.—As hereinafter used, the term "new company" will be understood to mean either the reorganized debtor or a new company created to take over the properties and assets of the several existing companies.

The effective date of the plan should be June 30, 1938. The obligations and capital stock of the Denver and the affiliated companies outstanding on that date, excluding intercompany holdings and securities under pledge, are listed in the appendix to this report. The total amount of debt shown, $171,374,879, is approximately $14,318,000 in excess of that outstanding on December 31, 1936, the date when the filed plans were to become effective, and such increased obligations must be provided for. Under the provisions of section 77 (d) we may, after public hearing, approve a plan which may be different from any which has been presented and will, in our opinion, meet with the requirements of subsections (b) and (c) and be compatible with the public interest.

The capital structure of the new company which we approve as meeting the requirements of the act, and the allocation of new securities to the holders of certain classes of claims, are shown in tabulated form in the appendix which also shows the principal amounts of securities, excluding those which may be issued for pledge, and the annual charges thereon.*

The record contains data showing the earnings of the system lines between 1927 and 1936, inclusive, and various analyses made from these data, as already described. Among the significant facts are the average annual income available for interest in 1934–36, after intercompany eliminations, amounting to $3,118,197 a year, that of the constructive 12-month period used by the debtor, amounting to $3,926,223, and the 1932–35 average of $3,606,920 a year, to which the committee applied a coverage factor of 1.3 and arrived at $2,774,554 as the allowable amount of new fixed interest charges. This was considered by the committee a reasonable measure of the probable low range of future earnings. Reference was made to indications that the revenues of 1937 would exceed those of 1936 and that the trend would continue upward. The testimony may have tended to support such a view, but the facts as later reported to us are that the combined income of the Denver and the Salt Lake available for interest approximated $296,000 in 1937 and $673,000 in 1938. The Denver's own operation resulted in a deficit of $186,290 in 1937 and an available income of $223,356 in 1938. The plan recommended by the examiner was predicated on the record up to the close of 1936. But the sub-

* Appendix is omitted in this printing.

sequent decline in earnings, even though common to many roads in the same period, cannot be entirely ignored in a consideration of the question of new fixed charges. Neither should the reorganization proceeding be subjected to undue delay pending a demonstration that the carriers can again earn more than $3,000,000 a year. As we regard the situation, the initial issue of new first-mortgage bonds should be restricted to the minimum financing requirements of the reorganization. Subject to adjustment for conditions which cannot be determined until later, the amount of new first-mortgage 4-percent bonds contemplated under our plan and apparently necessary as shown in the following discussion, is $29,403,144, and the fixed interest charges on such bonds, the equipment-trust certificates, and the indebtedness to the Chase National Bank and the Railroad Credit Corporation, will amount to approximately $1,348,536 per annum. This sum exceeds the average income of $1,128,869 available during the 3-year period 1936–38, the period of lowest system earnings during the last decade, and in our opinion should not be increased. Studies have been made to ascertain the effect of deferred maintenance on the property in previous years which was in part made up by the expenditures for maintenance in 1936–38. While necessarily giving approximate results, these studies indicate that the average system income available for interest during the 3-year period, as adjusted, was about $2,893,255. Under the plan herein approved the fixed interest requirements, plus the maximum payment into the capital fund, would amount to $2,098,536, subject to some possible increase in the amount of first-mortgage bonds issued in the reorganization, as has been indicated. Thus, on the basis of the adjustments shown, the earnings of the 3-year period 1936–38 would provide a coverage of 1.38 for those charges. In giving this consideration to the low earnings in recent years our position is not that the system lines will never regain their former earning power, or exceed it, but rather that, with the present conditions in the railroad field and in the public interest, a conservative policy should be followed in deciding what level of income to take as the reasonably assured earning power of the system, as such level affects the amount of fixed interest charges to be permitted in the future. We find that, after due consideration of the probable prospective earnings of the properties in the light of their earnings experience and other relevant facts, there will be adequate coverage of these fixed charges of the new company by the probable earnings for the payment thereof.

The above stated amount of new first-mortgage bonds represents the aggregate amount of the debt to the Finance Corporation, the sum necessary to redeem the Salt Lake bonds outstanding, the prin-

cipal amount of the Denver's trustees' certificates outstanding, and $1,000,000 to cover reorganization expenses, etc. If the financing necessary in connection with the last three items should entail a larger amount of bonds for pledging purposes, the stated total would be correspondingly increased, but the total actual debt upon which interest would be payable would not be increased unless it was found necessary to sell the bonds at less than par. Provision is also made in the plan for the possible issue of first-mortgage bonds for the purpose of refunding the existing bonds of the Northwestern Terminal Railroad Company if that should be found desirable.

The total debt of the new company under this plan would approximate $76,232,510, and the total capitalization $147,433,354, taking the no-par common stock at $100 a share. The total maximum annual charges ahead of the common stock would be approximately $5,758,639 per annum.

The basis for the limitation of annual fixed interest charges and capital-fund payment to about $2,098,536 has been stated. The total debt, including income bonds, should not only bear a proper relation to total capitalization but should be such as to render the payment of dividends probable, at least on the new preferred stock, under normal conditions of business, as far as such conditions can be estimated from the facts of record. This requirement is in justice to the bondholders who are to receive preferred stock in part settlement of their claims, and, is, moreover, desirable in order to promote the use of preferred stock as a means of financing. The total charges ahead of dividends on the preferred stock, under the plan herein approved, will be slightly in excess of $4,000,000, and the full dividend requirements on that stock will be about $1,665,000 a year. The $4,000,000 figure reflects an initial issue of approximately $42,000,000 of 4½-percent income-mortgage bonds, allocated as shown in the appendix. That such total charges, and the amount of new bonds to which they correspond, cannot be increased without serious detriment to the prospective value of the new preferred stock is plain from the carriers' earnings record. In no year since 1931 has the total income available for interest reached $4,000,000. The average available income for the years 1932 to 1935, inclusive, used as a basis by the committee, was $3,606,920. Practically the same amount is reached by averaging the nine years 1930 to 1938, inclusive, which include the high of $8,060,528 in 1930 and the low of $295,504 in 1938. The adjustments tentatively made in our studies for undermaintenance and overmaintenance, would reduce the average somewhat. The debtor's carefully prepared forecast for a future normal year is

not overlooked in this connection, but the trend of earnings since it was presented discourages reliance on the results of such a study. Even should these results be realized, the earnings on the new common stock would amount to only $1.20 a share.

As hereinbefore stated, the report of our Bureau of Valuation shows the cost of reproduction of the system properties, less depreciation, plus lands and rights, working capital, and net additions and betterments to December 31, 1936, as $147,717,268. In the light of all the evidence it is clear to us that the approved amounts of fixed-interest bonds, of total debt, including income bonds, and of preferred stock are the maximum amounts which should be allowed in the formulation of a sound plan.

The following provisions for the new bonds and stock; capital fund, sinking fund, means of future financing, etc., are based upon those incorporated in the committee's plan, with modifications where we disapprove the committee's suggestions or where those suggestions are inconsistent with the new capital structure. Such modifications consist chiefly of lengthening the term of both issues of bonds, making the income mortgage an open mortgage, placing the income periods and the payment of bond interest on an annual basis instead of a semiannual basis, changing the terms of the capital fund so as to make accumulations of unappropriated sums available for additions and betterments as well as interest on the first-mortgage bonds, making the new common stock of one class only, altering the function of the voting trust, and eliminating the provision for warrants, and modifying the restrictions on future issues of stock so as to facilitate the use of stock in future financing. With respect to any matters of detail not provided for herein it is to be understood that the reorganization committee, with the approval of the court, may determine the proper terms, provided that such terms shall conform to the plan herein approved.

Note—"(Here follows a description of the terms and conditions of the securities to be issued by the new company, together with provisions as to the order of application of available net income. Since these relate to a plan which was not approved, the subject matter is omitted here and reference is made to the description of new securities in the approved plan and the application of available net income in the order of June 14, 1943.)"

Formula, matters in dispute.—The major questions in this case in connection with the application of a formula for establishing the relative earnings of the several mortgage districts are (1) the period to be used as a basis; (2) the mileage to be assigned to the cut-off; (3) the treatment of the excess earnings of the Junction line; (4) the liens of the mortgages with respect to certain units

of equipment and the percent of value to be allowed for use of equipment; (5) the treatment of branch lines subject to the first lien of the refunding and improvement mortgage; and (6) the disposition to be made of the stock of the Utah Fuel Company. Also entering into the computations were the adjustment of revenues on the narrow-gage lines because of the fact that the average freight revenue per net ton-mile on those lines is approximately 1.45 times that on the standard-gage lines, an adjustment of the revenues of the D. & R. G. consolidated mortgage district because of the failure of the potato crop in the San Luis Valley in 1934–35, an allowance to the R. G. Western consolidated mortgage district for the assumed earnings of the Utah Fuel Company, and an allowance to the D. & R. G. consolidated mortgage district for the use of the shops at South Denver also used for repairs on equipment operating over other divisions of the system. More important matters as to which the parties are in disagreement involve the rights of the bondholders and other secured creditors to the payment of interest accrued from the date of filing the petition under section 77, the question of a special provision for the holders of bonds secured by mortgages on the western divisions of the Denver, the claims of the Finance Corporation, the equity of the debtor's present stockholders, and the future control of the new company. On all these matters the testimony, briefs, and oral arguments are exhaustive. It is impossible in this report to recite in detail the claims and contentions made by all the parties.

Certain interveners objected to the use of the test-period year ended June 30, 1935, as a measure of the earning power of the several divisions of the system on the ground that the debtor's adjustments of the actual revenues and expenses resulted in a constructive figure which, in any event, does not fairly represent the full effect of the establishment of the cut-off route. We are unable to see how such effect could reasonably have been ascertained. All the adjustments of the actual operating results were fully explained. The committee accepted the result as a basis for its formula, and most of the parties offered no objection to it. The study, in fact, represents 18 months of operations after the opening of the cut-off. Clearly the operating results in 1936, 1937, or 1938, when earnings were greatly reduced, would not afford a representative basis, assuming it practicable to employ these results in a new formula computation. We are of the opinion that great precision cannot be expected in such a matter and that the test-period basis of income available for interest, as adopted, is a reasonable basis for the distribution of earnings and the development of a plan.

The cut-off.—In its first analysis the debtor showed the income of the cut-off available for the payment of interest in the test period as $85,241. This amount, plus the earnings on the bonds, etc., pledged with the Finance Corporation being insufficient to cover the interest charges on the new bonds assigned to the Finance Corporation, the shortage was supplied from the earnings of two of the western mortgage districts. The second analysis, on the waybill basis, showed the earnings of the cut-off to be $370,246, and this is the result finally adopted by the debtor. Both the first and second analyses represent the allowance of 175 additional miles to the cut-off. The third computation was on a straight mileage basis and showed a deficit of $285,993 for the cut-off. The committee added to the net of the cut-off, on a straight mileage-prorate basis, 42 percent of the increase in net earnings which it would have under the 175-mile arbitrary, computed on the waybill basis. The test-period revenues involved with the cut-off consist of approximately $2,100,000 from overhead traffic and $1,340,000 from local traffic, the latter originating or terminating at points on the Denver. The overhead traffic formerly moved about 400 miles on lines west of Dotsero and 342 miles east from Dotsero to Denver, via Pueblo. The cut-off shortens the distance between Dotsero and Denver to about 167 miles. In dividing the test-period revenue from overhead traffic between the cut-off and the mortgage districts west of Dotsero on a mileage basis, the latter would obviously receive a large increase if the shortened length of haul east of Dotsero were used. The debtor believed that, since the western districts benefit by all new traffic that is attracted to the cut-off route, they are not entitled to the additional earnings computed on the basis of the actual mileage of the cut-off. The debtor also considered that, because of the large investment in the cut-off, that line is entitled to credit for all the revenue which formerly accrued to the old line via Pueblo. Other reasons given for allowing the 175-mile arbitrary include the alleged higher operating cost over the cut-off as compared with the Pueblo route, high maintenance costs on the cut-off and the undeveloped condition of that route during the test period, the rental of the Moffat Tunnel, the saving in mileage, and the desirability of having the earnings represented by the collateral held by the Finance Corporation support the proposed allocation of first-mortgage bonds to that creditor.

Despite the admitted detrimental effect of the diversion of traffic to the cut-off on the earnings of the old line east of Dotsero, and the validity of some of the objections raised to the theory followed by the debtor, e. g., increasing operating costs west of Dotsero due to meeting schedules on both routes, we are persuaded that

the use of the constructive mileage of the cut-off is justified on the ground alone that a lesser mileage would distort the earnings of the western mortgages. It is not clear how the D. & R. G. consolidated mortgage can be compensated for the construction of the other route to Denver, which tends to render the Pueblo route obsolete, without unduly expanding the new capital structure. The debtor takes the view that the private interest of the consolidated mortgage is subordinate to the public interest in the shortening of the haul. Some of the through traffic moving over the cut-off is new traffic which probably would not have come to the Denver if only the Pueblo route were available. The system as a whole should benefit ultimately from the cut-off operation, the economies from consolidating the several properties, and the saving in interest on the Salt Lake bonds.

Junction earnings.—The formula studies show the gross revenues of the Junction in the test period as $1,247,564, allowing for the 175-mile arbitrary for the cut-off, and as $1,396,826 on the basis of the straight mileage prorate. Under the committee's formula, allowing 42 percent of the 175-mile arbitrary, the net income of the Junction available for interest was $275,663.

The lease of the Junction property provided that 30 percent of the Junction's gross revenues be paid as rental but that the payment should in no event be less than the amount of the annual interest on the first-mortgage bonds, or $100,000 per annum. All the capital stock of the Junction being pledged under the refunding and improvement mortgage, the trustee under that mortgage argues that this mortgage is entitled to be credited with all the net earnings of the Junction after payment of interest on the bonds, up to 30 percent of its gross revenues. The trustee further contends that an agreement made by the boards of directors of the Junction and the Denver in 1925, which modified the lease by limiting the rental to $100,000 a year, is void. The debtor adopted this theory, crediting the net income of the Junction to the refunding and improvement mortgage.

The trustee of the D. & R. G. consolidated mortgage, as well as the Insurance Group committee, claims that the earnings of the Junction should be allocated to the consolidated-mortgage bonds because the after-acquired-property clauses in the consolidated mortgage cover the leasehold estate in the Junction property vested in the principal debtor as the result of an agreement dated December 24, 1889. This agreement provided for the making of a formal lease covering the same subject matter as the agreement. No formal lease was subsequently made. However, there seems to be no reasonable doubt, considering all the terms of the agreement, and

the fact that the Denver has had some 47 years of occupancy under the agreement, that the effect of the agreement was to vest a leasehold estate in the principal debtor. See *Levin* v. *Saroff*, 201 Pac. 961 (Cal. App.); *People* v. *Saint Nicholas Bank*, 3 N. Y. App. Div. 544 (affirmed 151 N. Y. 592). Under Colorado law, a lease of land is regarded as real property. *Bonfils* v. *McDonald*, 270 Pac. 650.

The D. & R. G. consolidated mortgage, dated July 15, 1886, conveyed to the trustee—

> All the property real, personal, and mixed * * * of every kind and description, now owned or hereafter to be acquired, including its entire line of railroad now owned or hereafter constructed" * * * "together with all the estate, right, title, interest, property * * * as well at law as in equity, present and future * * *.

The mortgagor agrees to make—

> all such further acts, deeds, conveyances, * * * for the better carrying out the purposes hereof, and assuring unto the said Trustee * * * in the trust hereby created, upon the trusts and further purposes herein expressed or intended, all and singular the lands, * * * property, railways, * * * lease holds * * * now owned * * * or subsequently to be acquired, * * * and all other property and things whatsoever, which may be hereafter acquired, in aid of or by way of substitute for, or for use for the purposes of the same * * *.

It may safely be concluded therefore that the leasehold estate in the Junction property became subject to the lien of the D. & R. G. consolidated mortgage. This lien is secondary to the Junction first mortgage dated December 1, 1889, but because prior in time it is prior to the mortgage created by the Junction on January 1, 1929, which, together with the stock of the Junction, is pledged under the refunding and improvement mortgage.

The situation as to the Junction stock is substantially this: One of the predecessors of the principal debtor, having acquired in 1889 a leasehold of the Junction property, pledged it as of July 15, 1886, under the D. & R. G. consolidated mortgage of that date. Many years later, in 1924 or thereabouts, the debtor, being the owner of the stock of the company (the Junction) which had conveyed the leasehold estate, pledged that stock as additional security for the refunding and improvement mortgage. The trustee of that mortgage points out that subsequent to the creation of the mortgage the debtor, through its ownership of the capital stock of the Junction, caused the lease to be modified by (1) decreasing the rental from 30 percent of the gross revenue, with a minimum sufficient to pay the interest on the $2,000,000 of the Junction bonds, and (2) transferring the obligation to pay for additions, betterments, and improvements from the debtor to the Junction. Through the

latter arrangement the Denver was able to use funds obtained from the sale of refunding and improvement bonds for the additions, betterments, and improvements on the Junction, and to have the Junction issue its bonds for that amount ($906,000), which bonds were then pledged under the refunding and improvement mortgage. The trustee of that mortgage argues that these transactions rendered the Junction securities pledged under the mortgage practically worthless, that the transactions were void as being in violation of the purposes and spirit of the refunding and improvement mortgage, and that full effect must therefore be given to the lease in its original form. In our opinion, there is no merit in these contentions. The refunding and improvement mortgage authorized the debtor, without the consent of the trustee—

> from time to time to change, amend, * * * in whole or in part, any leases whose terms do not extend beyond the latest date of maturity of the refunding bonds at the time outstanding, or any leases whatever their term to or with a lessor which, at the time, is a controlled company of the railroad company, or any trackage rights, or any contracts relating to the mortgage premises.

That mortgage also permitted reimbursement out of the proceeds of the refunding and improvement bonds for additions, betterments, or improvements or real property owned by a corporation 90 percent or more of the capital stock of which was pledged thereunder, provided that bonds of such corporation, in principal amount at least equal to the amount of such expenditures, were pledged under the refunding and improvement mortgage. The mortgage also authorized the debtor to vote pledged stock for all purposes not inconsistent with the provisions or purposes of the mortgage.

We conclude that any earnings of the Junction during the test period in excess of the interest on its first-mortgage bonds should be credited to the D. & R. G. consolidated mortgage.

Equipment.—The chief controversy with respect to equipment involved the question whether certain equipment, having a depreciated value of $1,263,265,[5] as of December 31, 1936, is subject to the lien of the D. & R. G. consolidated mortgage or to that of the debtor's refunding and improvement mortgage. The trustee of the latter mortgage, in view of the complex problems of fact and law involved in a judicial determination of the matter, has accepted the committee's allocation of this equipment to the lien of the D. & R. G. consolidated mortgage, and no definite objection to such allocation has been presented by the other parties. Without attempting to decide this question on legal grounds, we think the

[5] As stated by the trustee of the refunding and improvement mortgage. The amount used by the committee was $1,333,252, as of December 31, 1935.

plan may properly give effect to the committee's allocation as a compromise reached by the principal interest affected. On such basis the depreciated book value of the equipment subject to the direct first lien of the refunding and improvement mortgage as of December 31, 1936, was $6,005,357, and that of the equipment subject to the first lien of $1,805,000 of equipment-trust obligations, was $6,575,955. The aggregate depreciated value of the standard-gage equipment covered by these liens was $11,408,021. Such equipment constituting nearly two-thirds of all standard-gage equipment on the debtor's system, the refunding and improvement mortgage trustee contends that, if such equipment is to be placed under the lien of a new first mortgage, the holders of refunding and improvement mortgage bonds should receive appropriate amounts of the new first-mortgage bonds. Approximately 70 percent of the refunding and improvement mortgage equipment is used on the R. G. Western and Junction lines.

The second matter in dispute is the adoption by the debtor in its formula, and by the committee in its plan, of a rate of 2 percent per annum applied to the estimated depreciated value of equipment used on each mortgage district. On this basis the committee computed the test-period earnings of the refunding and improvement mortgage equipment at about $118,000. In support of the 2-percent rate the debtor stated that the return on its investment in road and equipment during the test period was about 1.25 percent, and that, giving effect to the extra value of equipment because of its mobile nature, and the fact that the equipment was taken at depreciated value, a rate of 2 percent was considered fair. This conclusion is defended by counsel for the committee who argue that the equipment is not in fact available for movement generally but is part of the corpus of the estate and is entitled to earn only what the estate can earn. Moreover, counsel contend that the depreciated book value used is much too high, in that the element of obsolescence has not been considered. The trustee of the refunding and improvement mortgage presented an exhaustive analysis which among other things included computations of earnings on investment, based on adjusted income figures, and the cost of reproduction of the properties, less depreciation, plus the value of lands and rights. These computations showed earnings ratios of 2.94 percent and 2.79 percent for the test period based on the elements of value of the property, as reported by the Bureau of Valuation, with certain adjustments. The record contains a statement of 28 issues of equipment-trust certificates in 1936 by various railroad companies, the average interest rate being slightly in excess of 3 percent. The trustee shows that the average rate on the debtor's equipment-trust

obligations was about 5 percent. It calculates the average return in the test period on the mortgage divisions which use the refunding and improvement mortgage equipment at 4.514 percent, this being a weighted average representing the proportionate use of such equipment by these divisions. The trustee further refers to the reports of division 4 in *New York, N. H. & H. R. Co. Reorganization*, 224 I. C. C. 725, and *Chicago, I. & L. Ry. Co. Reorganization*, 228 I. C. C. 209, in which division 4 approved rates of return on equipment equal to the prevailing rates on the carriers' equipment-trust certificates, viz, 4½ percent and 5 percent, respectively. As indicated in the New Haven report, a rate between 4 percent and 6 percent is in accordance with established practice between railroads. In the present case we are of the opinion that for the purposes of this plan an increase of the 2-percent rate used in the formulas to a rate of 4 percent, which the trustee indicates will be acceptable to it, is fully justified.

Branch lines.—The financial result of operating the branch lines subject to the first lien of the refunding and improvement mortgage affects the ascertainment of the earnings of that mortgage district. The standard-gage branches are 13 in number, totaling about 86 miles, including the Pacific mine and Hooper-Cox branches, not in operation in the test period. The operating loss from these lines, as calculated by the debtor and the committee, was approximately $40,000 during the test period. On account of such ascertainment of loss, the amount of first-mortgage and income-mortgage bonds issuable to the holders of the refunding and improvement mortgage bonds was reduced about $870,000 by the debtor and about $1,000,000 by the committee. The system revenue contributed by these branches approximated $1,500,000, which, according to the mortgage trustee, yielded approximately $1,000,000 of net revenue.

The trustee under the mortgage attacks the debtor's and the committee's estimates of loss on the branches principally on the ground that an unduly small proportion of the revenues was credited, and an unduly large proportion of the system taxes were charged. The trustee undertook to show that, by giving the branches a 15-percent division of the revenues and by adjusting operating expenses and taxes, the net earnings of the branches would be about $100,000. The data used were admittedly incomplete, and the methods followed were shown to be questionable by counsel for the committee. Such earnings from the branches cannot be considered as established, but on the other hand, in view of the large amount of system revenue derived from the traffic orig-

inating or terminating at stations on the branches, the propriety of charging them with a substantial loss may be doubted. We consider it fair under the circumstances to disregard the alleged loss on the branches in dealing with the refunding and improvement mortgage bonds.

Utah Fuel Company.—Reference has been made to the data of record in connection with the value of the Utah Fuel Company stock. The pledging of the 100,000 shares of this stock with the trustee of the R. G. Western consolidated mortgage was described in the report of division 4 in *Denver & R. G. W. R. Co. Reorganization*, 82 I. C. C. 745, 753, and in the report of the Commission in the same proceeding, 90 I. C. C. 141, 148. The title to the stock is vested in the Missouri Pacific and Western Pacific, which by an agreement dated December 20, 1924, provided for a voting trustee and the payment of any dividends to the debtor so long as any accumulated dividends on the debtor's preferred stock remain unpaid.

In allocating earnings to the mortgage districts the debtor credited the R. G. Western consolidated mortgage with $83,333 from the fuel company's stock, by arbitrarily spreading a $250,000 dividend, which was declared out of capital in 1933, over three years, and the debtor's principal witness considered that treatment as adequate to absorb the whole value of the fuel company's stock. The committee allowed the R. G. Western consolidateds $567,448 of new income bonds, based on the earnings and so-called control value of the fuel company.

The trustee of the mortgage objected strongly to these appraisals, citing the report made by the mining expert. He filed exceptions to the examiner's proposed report, with respect both to the new securities assigned therein to the R. G. Western consolidated bonds and to the proposed provision that the Utah Fuel Company stock be pledged under the mortgage securing the new income bonds. The trustee suggests that the stock and its dividends be pledged as additional security for a special issue of new income bonds and that all of such bonds be assigned to the R. G. Western consolidateds.

Counsel for the debtor suggest that the parties agree to a distribution of the fuel company's stock among the holders of the R. G. Western consolidated-mortgage bonds on terms that might be found reasonable. Such a distribution seems to us fair in principle, especially in view of the provision of our plan whereby these bondholders will receive no new bonds and the fact that both the

debtor's and the committee's plans gave these bondholders the benefit of the fuel company's earning power, as they estimated it. In our view, the plan approved by us should provide that the trustee under the mortgage securing the R. G. Western consolidateds be permitted to obtain the release of the equities of redemption in the stock, and distribute the stock among the holders of bonds in any manner acceptable to them, or to enforce its rights as pledgee of the stock, the mortgage being in default, the proceeds recovered to be distributed to the holders of the bonds.

Accrued interest.—The debtor's plan recognizes accruals of interest on secured debt only to the extent that it was earned subsequent to the date of filing the petition under section 77, thereby eliminating about $4,770,000 of interest accrued to December 31, 1936. Even as to the portion of the interest that was earned, the debtor offered securities junior in rank to those allocated to the principal obligation. Counsel contend that interest after the basic date, i. e., the filing of the petition, is not allowable unless the estate is found to be solvent and an equity in the stock exists; that all claims must be dealt with as of the basic date; that a continued accrual of interest should not be allowed to wipe out a debtor's equity or to distort the relationship of claims. This is part of the debtor's general argument in connection with the equity of the present stockholders and the applicability of the composition principle in reorganization cases.

The debtor's mortgages provide that principal and interest are equally secured by the lien, and it seems evident that any interest accrued at the prescribed rates and remaining unpaid is as much a part of the debt as the principal. We are unable to agree with the debtor's view that the secured claims must be dealt with as of the date of the filing of the petition. *Spokane International Ry. Co. Reorganization*, 228 I. C. C. 387, 233 I. C. C. 157, *Wickwire Spencer Steel Co.*, 12 Fed. Supp. 528, and *Ticonic National Bank* v. *Sprague*, 303 U. S. 406.

Mortgages on the western lines.—Because of the showing that the earnings of the Denver's western lines during the test-period year were more than adequate to cover interest charges on the bonds representing first liens on such lines, the debtor proposes that the Junction first 5's and the R. G. Western first-trust 4's be exchanged, in each case, for like principal amounts of new 3½-percent bonds issued under a mortgage secured by a first lien on the Junction property, the R. G. Western property, and the Denver's property lying between Dotsero and Rifle, and between Grand Junction and Crevasse, Colo., thus placing all lines west of Dotsero

under the direct lien of the new western-division mortgage. An additional amount of new 3½-percent bonds, or a corresponding payment in cash, is offered to compensate the bondholders for the loss of interest to maturity on the present Junction bonds and R. G. Western bonds. Such maturities are December 1, 1939, and July 1, 1939, respectively. It is contended by counsel for the debtor that the holders of the bonds in question should get all that they could receive in a liquidation or foreclosure. The relatively high earning power of these lines, even on the basis of the cut-off mileage used in the committee's formula, is uncontroverted.

The committee considers that "nothing can duly recognize the position of these bonds short of a new first-lien bond for the total of their principal and accrued unpaid interest, the new bonds to be of such interest rate, maturity, and terms as to sell at par." In order to meet this requirement, as has already been stated, the committee proposes the issue of new series-A bonds having a relatively short term, a permissible interest rate up to 4½ percent per annum, and other features intended to assure the required market value.

The Finance Corporation disapproved the creation of a separate western-division mortgage, because the new first and refunding mortgage bonds, which the debtor proposed to offer the corporation in settlement of its claim, would constitute only a second lien on the profitable western lines. The provision made for the western bonds by the committee was in the belief that a separate mortgage is unnecessary. The committee's proposal was apparently more acceptable than the debtor's to the trustee of the R. G. Western first mortgage and the Junction first mortgage, but the examiner's recommended plan, assigning new first-mortgage bonds, without special terms as to interest rate and maturity, was vigorously rejected by the trustee. Counsel for the committee concur in the position taken by the trustee, which is that any plan which does not recognize the preferred status of the western first-lien mortgages in the matter of earning power, and which does not give them preferred treatment, is inequitable, unfair, and would deprive the bondholders of their property without due process of law.

The advantages of new mortgages on the entire property of the system seems to us important from the standpoint of simplicity in the capital structure, from that of future financing, and as conducive to the cooperation of the Finance Corporation in effecting a consolidation of the lines and in general in carrying out the plan. The relative earnings position of the R. G. Western first-trust bonds and the Junction first-mortgage bonds may be recognized in

the allotment of new securities without the use of a separate mortgage. Under the capitalization which we consider permissible, however, it is impossible to assign new first-mortgage bonds to these claims or to those of any of the debtor's bondholders. The holders of the bonds in question will receive new income-mortgage bonds in amounts equal to the total claim for principal and interest as of the effective date of the plan, and the holders of bonds secured by mortgages on other parts of the debtor's lines will receive lesser amounts of new bonds in accordance with the indicated earning power of the respective lines, as will be explained later. Proportional sacrifices on the part of the first-lien bondholders are essential to the consummation of a plan at this time. It is not a matter of successive liens on the same physical property but more in the nature of parallel liens, the treatment of which depends primarily on relative earnings.

Finance Corporation claims.—The obligation of the debtor and secondary debtor to the Finance Corporation, in total amount of $11,959,469, as of June 30, 1938, is secured by pledge of numerous securities, hereinbefore described, among which are the capital stocks of the Salt Lake, the Salt Lake Western, and the motor companies, $4,385,000 of the Denver's refunding and improvement mortgage bonds, $1,395,000 of the R. G. Western consolidated-mortgage bonds, and $1,266,000 of the Salt Lake income bonds. The Finance Corporation introduced a large amount of evidence to show that its claim is entitled to settlement in cash or in readily marketable securities, particularly in view of the independent earning power and value of the Salt Lake.

The treatment accorded the Finance Corporation in both the debtor's plan and the Insurance Group plan recognized the Finance Corporation claims as fully secured. These parties and others, however, filed exceptions to the examiner's proposed report, recommending the allotment of new first-mortgage bonds for the full amount of the claim, on the ground that such treatment was inconsistent with that recommended for the several classes of securities pledged to secure the loans, and that the proposed allocation of new first-mortgage bonds to the Finance Corporation was unduly liberal, resulting in an injustice to the present bondholders, particularly the holders of the R. G. Western consolidateds and the D. & R. G. consolidateds. The complaint arises more from the fact that the examiner reduced the aggregate amount of first-mortgage bonds from that contemplated under the plans filed than from any new concept as to the fully secured position of the Finance Corporation. The approval of the issue of new first-mortgage bonds to

the Finance Corporation, while the debtor's bondholders are to receive none of such bonds, is justified, in our opinion, by considerations beyond the estimated value of the particular securities under pledge. Not only is the Finance Corporation in possession of the stocks of the Salt Lake and the Salt Lake Western, and thus in position to veto the consolidation of properties which forms the basis of the plan, but it has indicated that it will, if satisfied with the plan, agree to underwrite the financing necessary to redeem the Salt Lake bonds outstanding in the hands of the public, the payment of trustee's certificates, and the cash required for reorganization expenses, etc., a total of $17,443,675.

It is probable that under present conditions the new first-mortgage bonds of the reorganized company would not be salable at par, and the Finance Corporation should be compensated in some manner for acceptance of them at par in return for furnishing the $17,443,675 of cash necessary to carry out the plan. But clearly such compensation should not be limited to the probable present deficiency in the market value of the bonds. A practicable development of the procedure for placing the plan in effect will require a definite commitment by the Finance Corporation prior to the referendum on the plan, and from six months to a year probably will elapse after such commitment before the Finance Corporation will be called upon to supply the funds. At the approximate time of the financing, the transaction must receive our approval under section 5 of the Reconstruction Finance Corporation Act. What the market value of the securities may be at that time obviously cannot now be forecast.

In view of these circumstances, we approve the exchange of new first-mortgage 4-percent bonds, series A, in the approximate amount of $11,959,469 in settlement of the claims of the Finance Corporation for principal and interest accrued to June 30, 1938, such arrangement, however, to be conditioned upon agreement by the Finance Corporation to purchase, at par, approximately $11,443,675 of series-A bonds, the proceeds to be used for the purpose of redeeming the $11,234,000 of Salt Lake first-mortgage bonds and income bonds outstanding, and further to purchase approximately $6,000,000 of such bonds for the purpose of paying the debtor's trustees' certificates outstanding, the expenses of the reorganization, and for working capital. In the event of failure of the Finance Corporation to file with the court, prior to a referendum on the plan, a commitment to supply the new money under the above-prescribed terms, the plan should be considered to be impracticable, and should be returned to us for further consideration.

Means of future financing.—In the debtor's plan, the means of future financing by the new company, with respect to requirements not covered by the additions and betterments fund and new equipment-trust obligations, are provided through bonds to be issued under any of the proposed mortgages, as well as through the new preferred stock. Counsel for the committee take the position that first-mortgage bonds offer the lowest yield and provide the cheapest forms of financing; that the preservation of a sound capital structure will be insured if the new mortgage imposes proper limitations as to the purposes and amounts of additional issues; that fixed-interest bonds issued under such conditions and the limitations prescribed in section 77 provide a continuing medium for investment in railroad securities by trust funds and trust institutions, and thus broaden the market for cheap credit. Counsel further contend that there is no necessity for a sinking fund for the retirement of bonds issued under an open first mortgage, such as is contemplated, and that any reduction in the amount of bonds issuable in order to provide for a sinking fund would be unjustifiable, "since it would require the bondholders to pay off their own debts for the benefit of the equity."

Counsel urge that, in the case of income-mortgage bonds which are issued to present bondholders having a vested contract right to the payment of both principal and interest, creditors receiving such bonds are entitled to the payment of the principal as soon as it may be done without prejudice to the property. Accordingly, a sinking fund for the retirement of income bonds, issued under a closed mortgage, is considered by them to be desirable, provided the annual payments are made after payments to the capital fund and of contingent interest.

While we consider the committee's proposal for the early retirement of the income bonds a proper one, it is doubtful that the financing medium of the new company by bonds should be restricted to first-mortgage fixed-interest bonds. The plan herein approved provides for a relatively small initial issue of such bonds and otherwise departs from the committee's plan, owing to a different consideration of the earning power of the property, as has been stated. We believe that it will be in the interest of the new company to have both the first mortgage and income mortgage open, with proper restrictions as to the purposes for which additional bonds may be issued.

Equity, future control.—The debtor's contention that the present stockholders have a substantial equity is based on the recorded investment in the property, the recent improvements, which are

expected to increase net revenues, and the alleged potential earning power of the road. Counsel argue that the bankruptcy of the company was a temporary condition due to the heavy investment in the cut-off, that depression earnings should not govern in determining the equity of the stockholders, that no consideration should be given to our valuation of the physical property, that real value can be fixed only by means of a sale, and that an administrative body has no power to foreclose a property interest by an appraisement. Counsel for the debtor believe that section 77 is a composition statute, under which an agreement with the creditors is contemplated, such agreement being subject to our approval only from the standpoint of fairness and the public interest.

Section 77 provides, among other things, that the plan must afford due recognition to the rights of each class of creditors and stockholders. In *New York, N. H. & H. R. Co.*, 16 Fed. Supp. 504, 511, *Northern Pac. Ry.* v. *Boyd*, 228 U. S. 482, 505, and other cases, the courts have ruled that the claims of bondholders holding liens on the property of a bankrupt estate must be satisfied before consideration can be given to the rights of the stockholders. In our opinion, section 77 contains no provision which is contrary to the law of the land in respect of the relative rights and priorities involved in such a case as this. The rights of creditors and stockholders may be modified under the provisions of section 77 (b) but certainly not in violation of recognized priorities as between senior and junior interests. It follows that we must consider the aggregate amount of the claims of the bondholders and other secured creditors in the light of the earning power of the system, past, present, and prospective, and all relevant facts, in order to determine the equity of any class of stockholders, this being essential to the findings which we may be called upon to make under section 77 (e) in connection with the question of submitting the plan to the stockholders. The requirements as to such findings are not consistent with freedom of the debtor to make an agreement with its creditors for a composition of their claims or with the assumption that the debtor's interest shall remain undisturbed regardless of the apparent insolvency of the company. If the evidence clearly indicates no equity for the present stockholders, we are unable to find justification for their participation in the plan.

Referring to the balance sheet of December 31, 1936, which is the latest one contained in the record, the capital liabilities of the Denver, other than capital stock, together with total current liabilities, deferred liabilities, tax liability, government grants, and other unadjusted credits, amount to $154,552,730. Deducting all book assets, other than those representing investments, the net

amount was $140,560,266. For the combined properties, after intercompany eliminations, the corresponding figure was $153,314,502, which represents the net debt of the system on the basis of the consolidated balance sheet.

The decline in earnings was most marked between 1931 and 1932. Considering the Denver's operation alone, the average income available for interest during the 5-year period 1927–31 was $7,090,618 a year. During the next four years, 1932–35, adopted as a basis for the committee's plan, the Denver's average available income was $3,025,728. During the succeeding three years, 1936–38, the average was only $685,974. As of January 1, 1937, the effective date of the plans presented, the Denver's total debt, including unpaid interest, amounted to about $146,262,723, and the annual charges on the principal only were $5,762,392 per annum. As of June 30, 1938, the effective date of this approved plan, the total debt, including interest, had increased to $160,140,879 and the annual charges to $5,919,227. In no year since 1930 have the Denver's earnings been equal to such charges. The Denver's part of the test period earnings was $2,431,217, and its part of the predicted earnings in the future normal year was $5,198,318. In no year has the present Denver Company paid a dividend on either class of stock.

Since the Denver controls the Salt Lake through ownership of over 99 percent of its capital stock, the combined earnings in connection with the combined debt may be considered as bearing upon the value of the equity of the Denver's stock. On this basis the average system income available for interest was $8,103,881 during the five years 1927–31, $3,606,921 during the four years 1932–35, and $1,128,869 during the three years 1936–38. The total system debt increased from $157,496,723 as of January 1, 1937, to $171,374,879 as of June 30, 1938, while the annual charges on the principal increased from $6,406,432 to $6,563,267. As in the case of the Denver alone, these charges have not been earned in any year since 1930, and are not equaled either by the earnings of the test period or by those shown for the normal year. There is no evidence in the record indicating any probability that the carriers can bring their earnings up to the 1930 level or to that of the 1927–31 average, and in our opinion such former earnings should not be relied upon as the measure of an earning power justifying a finding that the equity in the debtor's stock has a value. The forecast for a future normal year, showing $6,215,423 as the system income available for interest, compares with about $8,000,000 earned in 1930 and a slightly larger average amount in 1927–31. The forecast figure, if capitalized at 4½ percent, approximates $138,000,-

000, while the total debt exceeds $171,000,000. The reproduction-cost figure of $147,717,268 has been referred to. From all these considerations we find that the equity of the owners of the debtor's common stock and its preferred stock has no value and that the holders of claims in classes 1 and 2 are not entitled to participate in the plan.

While the Insurance Group committee concluded that there is no equity in either class of the debtor's stock, it proposed that the proprietary companies be given precedence in the right to acquire effective control of the new company by purchase of the proposed class-B common stock, as had been described. The Western Pacific is not represented in this proceeding, but the representatives of the debtor, the Missouri Pacific, numerous civic bodies, and others have strongly urged that our plan provide a means whereby the proprietary companies may retain control of the Denver through acquisition of a majority of the new voting stock. They contend that the plan would not meet the requirement of public interest unless it contained such a provision. The evidence in this connection includes facts as to the long-established through route via the Missouri Pacific, the Denver, and the Western Pacific, the dependence of the Missouri Pacific's line between Osawatomie and Pueblo on the through traffic which has been developed, the need of the Denver for both the Denver gateway and the Pueblo gateway, the grouping of the Missouri Pacific, the Denver, and the Western Pacific under our consolidation plan *(Consolidation of Railroads, supra)*, our approval of the acquisition by the Missouri Pacific from the Western Pacific of a half interest in the Denver's stock *(Denver & R. G. W. R. Co. Reorganization,* 82 I. C. C. 745), and other matters. It has been argued that to divide the proprietary interest in the Denver between the present stockholders and other trunk lines as suggested by the committee would destroy the existing working arrangement and result in injury to the Denver.

As we view the matter these are not questions for us to decide in promulgating a reorganization plan where we find that the present stockholders have no equity, and we do not consider it our duty in this case to decide for the new owners what affiliations with other systems will be most advantageous to the new company, or to fix a price for any stock which may be offered to the Missouri Pacific, Western Pacific, or other railroad companies. In order, however, to facilitate any reasonable plan which the new stockholders may adopt with respect to the acquisition of an interest by a larger system or systems, the following provision for the stock should be incorporated in the reorganization plan. All the common stock issued by the new company in the reorganization, excepting shares

issued to qualify directors, should be deposited under an escrow agreement with a bank or trust company designated by the court and escrow receipts issued to the persons entitled to receive such stock under the plan. The escrow agreement should be for a term of 10 years from July 1, 1939, and should provide that the reorganization committee, as voting trustees, may, subject to our approval, and with the consent of the holders of escrow receipts representing a majority of the shares on deposit, sell all or any part of such deposited common stock at such price or prices as they may deem advantageous to the interest of the new company and its stockholders. It should be provided that all holders of escrow receipts will be bound by the terms of any sale which shall have been approved by us and consented to by the holders of escrow receipts representing a majority of the total number of shares issued, and that the new proceeds of any sale, together with any unsold stock, shall be distributed pro rata among the holders of the escrow receipts. During the life of the escrow agreement, the holders of escrow receipts should have the right to receive notice of all meetings of stockholders and to direct the reorganization committee as to the manner in which the stock represented by such escrow receipts shall be voted at such meetings. In the absence of such directions, the deposited stock should be voted in such manner as the reorganization committee may determine.

Allocation of new securities.—In order to establish a distribution of the test-period earnings conforming to the conclusions reached above, the debtor's basic distribution (exhibit 109, note A) is adjusted to transfer the group of equipment in dispute from the refunding and improvement mortgage, as shown in the committee's formula, and to cancel the loss on the refunding and improvement mortgage branches and allow a return of 4 percent per annum on the standard-gage equipment subject to the lien of that mortgage, as shown in the computations made by the trustee. The resulting figures, representing test-period income available for interest, are as follows:

R. G. Western first-trust mortgage	$1,122,050
R. G. Western consolidated mortgage	[1] 88,419
Junction first mortgage	164,563
D. & R. G. consolidated mortgage	978,628
Equipment trusts	131,519
D. & R. G. W. refunding and improvement mortgage	333,297
R. F. C. collateral (earnings of the cut-off, Salt Lake's operation, motor carriers)	1,284,585
	3,926,223

[1] Deduction.

Referring to the last item above, if the interest requirement of the debt to the Finance Corporation, together with that of the new bonds to be issued for the redemption of the Salt Lake bonds, be subtracted from the allocated earnings of $1,284,585, an excess of $348,359 remains, which, in our opinion, should be distributed among the three mortgage divisions where the interest requirements were not covered by earnings, viz, the R. G. Western consolidateds, the D. & R. G. consolidateds, and the refunding and improvements, and should be distributed in proportion to their respective deficiencies. When this is done the earnings, other than those of the Finance Corporation division and the equipment trusts, are as follows:

	Percent
R. G. Western first-trust mortgage, $1,122,050	39.3
R. G. Western consolidated mortgage, $32,496	1.1
Junction first mortgage, $164,563	5.8
D. & R. G. consolidated mortgage, $1,124,632	39.3
D. & R. G. W. refunding and improvement mortgage, $414,837	14.5
	100.0

If the above percents be applied to $42,000,000 of new income-mortgage bonds, being the approximate aggregate amount of such bonds which we find to be justified by existing conditions, the resulting amounts would bear the following relations to the amounts of the five claims, respectively: R. G. Western first trusts, 95.3 percent; R. G. Western consolidateds, 2.7 percent; Junction firsts, 105.5 percent, D. & R. G. consolidateds, 35 percent, and D. & R. G. W. refunding and improvement mortgage bonds, 36.5 percent. The distribution of new income bonds, shown in the attached appendix, is in substantial accord with these percents and in our opinion provides for an equitable treatment of the several claims based on the data available.

The new company should assume the equipment obligations of the present companies, or their trustees, at the consummation of the plan. We find that the interests of the holders of equipment obligations will not be adversely and materially affected by the plan of reorganization approved by us, and submission of the plan to such holders is not necessary. The issue of additional equipment obligations prior or subsequent to the consummation of the plan, if duly authorized under section 20a of the Interstate Commerce Act, is not prohibited under the plan herein approved.

The holders of bonds of the classes stated below should receive for each $1,000 bond and all unpaid interest thereon, as of the effective date of the plan, the following approximate amounts of new securities: R. G. Western first-trust bonds, $1,140 of new

4½-percent income bonds; R. G. Western consolidated-mortgage bonds, $1,150, par value, of new 5-percent preferred stock; Junction first-mortgage bonds, $1,154 of new 4½-percent income bonds; D. & R. G. consolidated-mortgage 4-percent bonds, $406 of new 4½-percent income bonds, $290, par value, of new 5-percent preferred stock, and 4.64 shares of new common stock; D. & R. G. consolidated-mortgage 4½-percent bonds, $413 of new 4½-percent income bonds, $295, par value, of new 5-percent preferred stock, and 4.75 shares of new common stock; D. & R. G. W. refunding and improvement mortgage 5-percent bonds, $416 of new 4½-percent income bonds, $297, par value, of new 5-percent preferred stock, and 4.75 shares of new common stock; D. & R. G. W. refunding and improvement mortgage 6-percent bonds, $429 of new 4½-percent income bonds, $306, par value, of new 5-percent preferred stock, and 4.9 shares of new common stock; D. & R. G. W. general-mortgage bonds, 4.15 shares of new common stock. The holder of each $1,000 Junction first-mortgage bond should receive, in addition, a cash payment of $14.17, representing 17 months' interest on such bond at 1 percent.

The foregoing amounts of new securities, being mostly in odd figures, owing to the accumulations of interest on the present bonds and other circumstances, will require the issue of scrip for sums less than $100 in the case of bonds, and for fractional shares of stock. Provision for the issue of such scrip should be made in the plan.

The holders of the 460 shares of stock of the Salt Lake outstanding in the hands of the public should receive, in exchange therefor, $46,000, principal amount, of new 4½-percent income bonds. The system earnings of the test-period year, as computed by the committee, correspond to approximately $4.21 a share for the Salt Lake stock, but the highest actual earnings of the Salt Lake in any one year since 1929 were only $1.79 a share, and in other years since 1929 they were much less than $1 a share. One intervener computes the test-period earnings on the Salt Lake stock at $8.07 a share after giving effect to the estimated savings from consolidation, as well as the savings through the proposed refunding of the Salt Lake bonds on a 4-percent basis. While the proper treatment of this stock is debatable, the use of the test-period earnings is consistent with the approved plan, on which basis we consider the allocation of new income bonds to this claim, as proposed in the debtor's plan, to be fair.

The secured note held by the Railroad Credit Corporation should either be paid in cash or be extended, at the discretion of the reorganization committee. If the latter plan be adopted, the note

of the new company should be in face amount equal to the indebtedness to the Credit Corporation, after any distributive credits which may apply thereon, bearing interest at the contract rate per annum, and payable in 6 months from the effective date of the plan. The new securities issuable as collateral for such note, representing those for which the present collateral with accumulated interest would be exchangeable under this plan, would consist of $268,772 of new income bonds, $191,980 of new preferred stock, and 3,072 shares of new common stock. Upon payment of such note the pledged securities should be canceled. Nothing in the foregoing provisions is intended to limit or in any manner affect the right of the Railroad Credit Corporation to apply, in its discretion, the income on and proceeds of the collateral held by it to or toward the payment of the principal or interest, or both, of or upon its claim against the debtor prior to the consummation of the reorganization.

The secured note held by the Chase National Bank should be canceled and a new note or new notes issued in face amount equal to that of the present note, plus interest accrued to June 30, 1938, in the amount allowed by the court, such notes to mature in 10 years, subject, however, to renewal or renewals from time to time at the option of the new company for further periods of 10 years each until retired in the manner to be set forth in the agreement securing such notes. Such notes should bear interest at the rate of 4 percent per annum, payable semiannually on October 1 and April 1 of each year, but such interest should be contingent on, and payment thereof should be limited to, the total of the interest and dividends paid by the new company on the collateral securing such notes. The interest should be cumulative to the maximum amount at any one time of 16 percent, whether for consecutive or nonconsecutive income periods. Any interest and/or dividends paid upon the pledged collateral in excess of interest requirements on such notes, including accumulations of interest, should be applied to the payment of the principal amount of such notes. Such notes may be redeemed in whole or in part at any time on 30 days' notice at their principal amount plus full interest at the rate of 4 percent per annum accrued since the last preceding April 1, and all unpaid accumulated interest. Upon the payment or other retirement of all such notes, the collateral securing them should be returned to the new company, and the new company should, in the case of certificates of stock, cancel and retire the same, and in the case of bonds deliver the same forthwith to the trustee under the indenture securing the same for cancelation and retirement; no bonds should be issued in lieu of any bonds so canceled and retired. The

new securities issuable as collateral, representing those for which the bonds now pledged, with accumulated interest to the effective date of the plan, would be exchangeable under the approved plan, would consist of $2,533,650 of income bonds, $1,809,750 of preferred stock, and 28,956 of common stock.

As has been stated, the Salt Lake bonds should be called for redemption as a part of the plan, the call price for the first-mortgage 4's being 101 and that for the income-mortgage 6's being 102. The trustees' certificates outstanding, which represent a lien prior to the lien of any of the mortgages issued or assumed by the debtor, should be paid in cash. Additional cash in the approximate amount of $1,000,000 should be provided for the payment of the expenses of reorganization and for working capital. As the needs of the company at the time the reorganization may be effected are not ascertainable, the provision for $1,000,000 of cash is necessarily tentative. The total requirements mentioned in this paragraph aggregate approximately $17,443,675, against which a like amount of new first-mortgage 4-percent bonds are shown in the plan schedule. In discussing the claims of the Finance Corporation we have already stated that a commitment should be obtained from that corporation obligating it to provide the financing described by taking the new first-mortgage bonds at par as a condition of the issue of new first-mortgage bonds for the full amount of the claim of the Finance Corporation.

As of December 31, 1936, there were outstanding $278,297.50 of coupons on bonds and equipment-trust certificates which had not been presented for payment prior to November 1, 1935. The cash item in the balance sheet included $105,891.06 for the payment of bond coupons. In the absence of later information it is assumed that not all these coupons will have been presented at the consummation of the reorganization and that the plan should make provision for them. Our order of approval will provide that such coupons shall be paid in cash by the new company if and when presented by the holders thereof.

Securities issued in the reorganization of 1924, which have not been claimed, should receive new securities under the plan herein approved, to the same extent as like outstanding securities of the Denver, or a cash settlement, as may be determined by the court.

Miscellaneous provisions.—The new company should assume liability for and pay in due course any and all taxes due to the United States from the debtors or their trustees or any of their subsidiaries, for any taxable period prior to the date of confirmation of the

plan, without proof thereof and without prejudice by reason of not having been proven.

As has been stated, the Moffat Tunnel Improvement District raised various objections to the plans of reorganization presented insofar as they provide for the merger or consolidation of the Salt Lake with the new company. It questions the authority of the court and this Commision to include in a plan of reorganization provision for the merger or consoiidation of the Salt Lake with the properties sought to be reorganized, on the ground that that corporation is solvent, is not a debtor herein, and a majority of its capital stock is pledged with the Finance Corporation as security for loans, with voting rights in the pledgee. Section 77 (b) describes in comprehensive language the subject matter which a plan of reorganization may embrace, stating that it may include "the merger or consolidation of the debtor with another corporation or corporations." We do not construe this to mean that every corporation that may be merged or consolidated with another by the plan need be a debtor or that its property need be subject to the jurisdiction of the court in the proceeding, provided that appropriate corporate action be taken by the nondebtor corporation.

The Tunnel District also takes the position that by reason of the existing lease for the use of the railroad tunnel the Salt Lake does not have the right by voluntary corporate action to cause its properties to be merged or consolidated with those of another corporation, contending in effect that the lessor is entitled to look to the property of the lessee as a trust fund for the payment of rent provided under the lease. We are not persuaded that these are legal consequences resulting from the lease. In *Kansas City Term. Ry. Co.* v. *Central Union Trust Co.*, 294 Fed. 32, the Circuit Court of Appeals, Eighth Circuit, held that contracts between railroad companies relating to joint ownership, maintenance, and use of a union station, which did not purport to be mortgages or to convey any title or interest in the properties of the several companies, did not create a lien on the general property of a company which took precedence of a subsequent mortgage and did not create covenants which ran with the property of the several companies and followed it into the hands of subsequent purchasers. In *Wabash, St. L. & P. Ry. Co.* v. *Ham*, 114 U. S. 587, the Supreme Court took occasion to discuss the so-called trust-fund theory in holding that equipment-trust obligations unsecured by any mortgage of a railroad company which subsequently consolidated with other corporations did not create a lien upon the properties of the consolidated company. Justice Gray said, in part:

The property of a corporation is doubtless a trust fund for the payment of its debts, in the sense that when the corporation is lawfully dissolved and all its business wound up, or when it is insolvent, all its creditors are entitled in equity to have their debts paid out of the corporate property before any distribution thereof among the stockholders. It is also true, in the case of a corporation, as in that of a natural person, that any conveyance of property of the debtor, without authority of law, and in fraud of existing creditors, is void as against them. * * *

But upon the consolidation, under express authority of statute, of two or more solvent corporations, the business of the old corporations is not wound up, nor their property sequestrated or distributed, but the very object of the consolidation, and of the statutes which permit it, is to continue the business of the old corporations.

The Tunnel District contends further that any transfer by the Salt Lake to the reorganized and consolidated company of its property and the lease would not be legal in view of a provision in the act of the legislature of the State of Colorado authorizing the construction of the tunnel and regulating its uses which reads:

All contracts may be assigned or subleased, *provided*, that the original contracting parties shall not be thereby relieved of any obligations under said contract or lease.

The lease, however, makes provision that successors and assignees of the lease shall be bound by the terms of the lease and that the lessee shall be released therefrom upon approval of said assignments by the lessor. This provision of the lease and the quoted portion of the statute were construed by the Circuit Court of Appeals, Tenth Circuit, in *Moffat Tunnel Improvement Dist.* v. *Denver & S. L. Ry. Co.*, 45 Fed. (2d) 712. That court stated its conclusions thereon as follows:

The powers conferred upon the [Moffat Tunnel] Commission undoubtedly are broad enough to permit it to cancel an existing lease with the consent of the lessee, and make another. The clause objected to amounts to that; it may release the Railway in case of a sale of its properties, but it is not required to. Such clause does not render the lease void.

We do not believe that the statute which declared, in effect, that the tunnel should be put to the greatest possible use, and that leases should be assignable, could be construed to prevent a lessee such as the Salt Lake from consolidating its property under appropriate State and Federal authority with a large railway system, such as that of the principal debtor, and having the reorganized and consolidated company assume responsibility for the performance of the lease. The Tunnel District requests that we suggest some method in connection with a plan of reorganization by which the district, if it should cancel the present lease and make a new

one with the consolidated corporation, may receive the same measure of security which it now has from its present solvent lessee. This we are endeavoring to do. The capital structure under the plan we approve herein we believe requires conservative fixed charges in the light of the probable earning power of the properties. Rentals due under the lease of the tunnel will, of course, be payable as a fixed charge before any interest would be payable on the bonds of the new company. We have issued numerous reports and orders describing the purposes of the tunnel and opening the way for more complete use of it for railroad purposes. It is our view that a long-range view of its purposes and possibilities should not be obstructed by placing too much emphasis upon the solvency of the present lessee. In the last analysis, the success of that carrier is closely allied with the system with which it is now connected through stock ownership.

The new company may take any action with respect to the lease or agreement with the Northwestern Terminal Railroad Company as may be lawful under the terms thereof. As to all other agreements and executory contracts, including the existing lease agreement of the Salt Lake with the Moffat Tunnel Improvement District, the new company should be deemed to have assumed the obligations with respect to such agreements and contracts which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding and which shall not have been disaffirmed by the trustees of the respective estates with the approval of the court prior to confirmation of the plan, and the new company should also assume any executory contracts made by the trustees, with the approval of the court, which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding

Claims against the debtors and their subsidiaries entitled to priority over their respective mortgages, claims for taxes levied, assessed, or accrued against the debtors, their subsidiaries, or trustees, current liabilities and obligations incurred by the trustees during the reorganization proceedings, to the extent unpaid at the date of confirmation of the plan, and claims arising from the disaffirmance of executory leases or contracts of the trustees pursuant to orders of the court, in respect of which claims are filed or evidenced in accordance with orders of the court, should be assumed by the new company and paid in the usual course of business with the same relative priority as they now have with respect to other obligations of the debtor or its subsidiaries. When so treated, we find, such claims against the debtors, other than the obligations of trustees, and the interests of parties to agreements

and executory contracts with the debtors assumed by the new company, are not adversely and materially affected by the plan.

The holders of unsecured claims against the debtors arising prior to the filing of the petitions under section 77, not entitled to priority, should receive new common stock on the basis of one share for each $200 of claim allowed by the court.

We are of the opinion that a reorganization committee is necessary to carry out the plan and that it should consist of five members, two to be designated by the Insurance Group committee as representatives of the R. G. Western first-mortgage bonds, the Junction first-mortgage bonds, the D. & R. G. consolidated-mortgage bonds, and the R. G. Western consolidated-mortgage bonds, one to be designated by the trustee under the Denver's refunding and improvement mortgage, one by the trustee under the Denver's general mortgage, and one by the Finance Corporation as its representative. The reorganization committee may fill any vacancies created by death, resignation, or otherwise, preserving the representation of the several interests as before. The members of the committee should agree to serve without compensation, but its expenses should be paid by the new company, subject to the provisions of section 77 and the approval of the court, as part of the cost of the effectuation of the plan.

The reorganization committee should not be authorized to solicit deposits of securities or authorizations to represent security holders, except upon approval by us of the terms of such solicitation, pursuant to section 77 (p) of the Bankruptcy Act, as amended.

The method and procedure for effectuating the plan should be determined by the reorganization committee in its discretion, and the committee should also determine the form, and, to the extent not inconsistent with the plan herein approved, the provisions of all mortgages, bonds, coupons, charters, bylaws, stock certificates, escrow agreements, and all other instruments necessary or desirable in connection with the effectuation of the plan, subject to the extent now or at the time provided by law to the approval of the court and of this Commission, or other tribunal having jurisdiction in the premises.

The number of directors of the new company and the manner of their election should be determined by the reorganization committee and provided for in the new charter or in an amendment of the debtor's present charter.

The plan should be carried out by vesting the properties of the Denver and its affiliated companies, together with the property held by the trustees, either in the reorganized Denver corporation or in a new corporation created for the purpose of this reorgani-

zation, and by the execution by the reorganized or new company of the new mortgages and the issue by it of the new securities contemplated under the plan. The reorganized or new company should be deemed to have come into possession of the properties as of the effective date of the plan, June 30, 1938. The merger or consolidation of the Salt Lake should be effected in a manner to be determined by the reorganization committee, subject to our approval and that of the court.

The expenses of reorganization, as allowed by the court, subject to the provisions of section 77, should be paid in cash or assumed by the new company as a cost of administration prior in lien to the new securities issued under the plan.

In connection with the plan proposed by the Insurance Group committee we described the suggested provision for a sale of the debtor's and secondary debtor's properties in the event the holders of more than one-third in principal amount of any class shall not have accepted the plan within a period to be fixed by the reorganization committee. Such a provision may properly be adopted, since section 77 authorizes inclusion in a plan, as part of the provisions for it execution, a sale of all or any part of the property of a debtor at not less than a fair upset price, etc. We are unable to approve, however, the sale provision as suggested by the committee, and are of the opinion that the following provision is appropriate in this case.

If so ordered by the court, the plan, after it has been found fair and equitable and has been confirmed by the court, may be executed by the sale or sales, at not less than fair upset prices, to be fixed by the court, of all or any part of the property of the debtor and the secondary debtor, all on such conditions and in such manner as the court may direct. Upon any such sale or sales, the property and assets offered for sale may be purchased for the benefit of the new company by the reorganization committee, and in that event there shall be applied on account of the purchase price the distributive share of the proceeds of such sale of all securities the holders of which shall have assented to the plan, and of the securities, though not assenting to the plan, of all classes which shall have accepted the plan. If the property of the debtor or secondary debtor, or both, so offered for sale should be sold to others than the reorganization committee, the plan herein approved shall be deemed inoperative except insofar as provision is made therein for the sale of the properties as may be ordered by the court.

In the event of any such sale to the reorganization committee, it may in its discretion sell all or any portion of the new securities distributable under the plan in respect of securities of any creditor,

if neither such creditor nor the class to which such creditor belongs shall have accepted the plan, provided that creditors in a class which shall not have accepted the plan, and who themselves shall not have accepted the plan, shall have the right, if they shall so notify the committee within a period of 30 days after the confirmation of the sale, to assent to the plan and receive the securities allocated to them under the plan in lieu of their aliquot share of the proceeds of such sale. The proceeds of sale of securities may be used to pay the portion of the purchase price payable in cash on any such sale of the properties.

We find that the plan of reorganization and consolidation herein described, which differs from any of the plans presented, will meet with the requirements of subsections (b) and (c) of section 77 of the Bankruptcy Act, as amended, and will be compatible with the public interest. Modification of the accounts of the debtor and the other companies involved, as a result of the plan finally adopted, should be subject to our approval, and the new company should submit its journal entries for such approval before making its permanent accounting records.

In view of the provisions of subsection (f) of section 77, we will give consideration, when a plan is finally adopted, to the granting of such authorization as may be requisite and appropriate for the execution of the plan, including the issue of securities.

An appropriate order will be entered.

EASTMAN, *Chairman*, concurring in part:

I concur, except as indicated in my separate expression in *Western Pac. R. Co. Reorganization*, 233 I. C. C. 409, decided June 21, 1939.

MILLER, *Commissioner*, concurring in part:

It is apparent to me that the total capitalization authorized in this proceeding is too high, particularly when measured by the original cost of the property, less depreciation.

For reason stated in my separate expressions in previous reorganization cases, I do not approve a mandatory capital fund. *Western Pac. R. Co. Reorganization*, 233 I. C. C. 409.

My remarks regarding the desirability of setting up sinking-fund payments in terms of a percentage of earnings, conditions regarding the issuance of fixed-interest bonds, a participation provision rather than a cumulative requirement for income bonds, and the use of no-par-value preferred stock, are equally as applicable to this case as to those in which they were made. *Spokane Interna-*

tional Ry. Co. Reorganization, 233 I. C. C. 157, and *Western Pac. R. Co. Reorganization*, *supra*;

SPLAWN, *Commissioner*, concurring in part:

I agree with the findings of probable earnings for the future. The discussion of priorities is difficult to follow. Apparently an effort is made to substitute for bonds on which interest is now being earned a security which will obviously have much less value. It is not made clear that such a substitution would be lawful.

INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

Submitted December 1, 1939. Decided April 2, 1940

Upon further consideration, plan of reorganization for the Denver & Rio Grande Western Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, modified and approved.[1]

Appearances as in prior report, and *A. Marvin Braverman, Claude E. Hamilton, Jr., A. M. Lewis, Curtis Heath, Samuel M. January,* and *George John Miller.*

Report of the Commission on Further Consideration

BY THE COMMISSION:

By our report and order of July 11, 1939, in this proceeding, 233 I. C. C. 515, we approved a plan of reorganization for The Denver and Rio Grande Western Railroad Company, debtor, and The Denver and Salt Lake Western Railroad Company, secondary debtor. Proceedings for reorganization of these companies are pending in the United States District Court for the District of Colorado. The plan provides that the properties of the debtor, the secondary debtor, The Denver and Salt Lake Railway Company, The Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company should be merged or consolidated by transfer of the subsidiary properties to the reorganized debtor or by transfer of all the properties to a new corporation organized for the purpose. The abbreviated titles used in our prior report will be used herein.

On or about September 9, 1939, petitions for modification of the approved plan were filed by (1) George S. Van Schaick et al. as the executive committee of a group of life-insurance companies,

[1] Previous reports, 212 I. C. C. 105 and 709, 217 I. C. C. 191, 224 I. C. C. 574, and 233 I. C. C. 515. Orders entered without report (other than orders permitting interventions), January 21, August 8, and September 4, 1936, January 9, April 12, May 26, and October 27, 1937, May 26 and November 28, 1938, and October 12, 1939; certificate, December 20, 1939.

known as the insurance-group committee, (2) Guy A. Thompson, trustee of the Missouri Pacific Railroad Company, (3) the Central Hanover Bank & Trust Company, trustee under the first-trust mortgage of the Rio Grande Western Railway Company and the first mortgage of the Rio Grande Junction Railway Company, (4) the United States Trust Company of New York, trustee under the consolidated mortgage of the Denver & Rio Grande Railroad Company, (5) the Guaranty Trust Company of New York, successor trustee under the first consolidated mortgage of the Rio Grande Western Railway Company, (6) the City Bank Farmers Trust Company, trustee under the general mortgage of the Denver & Rio Grande Western Railroad Company, (7) the Moffat Tunnel Improvement District and the Moffat Tunnel Commission, and (8) the Security Research Bureau, all interveners herein, and by (9) the debtor and its subsidiaries.

Certain interveners requested that the proceeding be reopened for further hearing, if such further hearing was deemed necessary by us, and that permission be given to file briefs and to present oral argument in support of the petitions. By order of division 4, all parties to the proceeding were permitted to file briefs on or before November 15, 1939, and reply briefs on or before December 1, 1939. Briefs were filed by the insurance-group committee, the Central Hanover Bank & Trust Company, the United States Trust Company of New York, the Guaranty Trust Company of New York, the City Bank Farmers Trust Company, the debtor, and the Untermyer family group; and reply briefs were filed by the Chase National Bank of the City of New York, the Finance Corporation, the Security Research Bureau, and the Moffat Tunnel Improvement District and the Moffat Tunnel Commission. We have given careful consideration to the questions raised by the parties and the modifications of plan requested.

Of chief importance among the modifications sought is that asking us to eliminate from the plan all provisions for consolidating the debtor with its subsidiaries. In urging this change, the insurance group committee contends that a consolidation of the Salt Lake with the Denver, in connection with the reorganization, upon the terms approved by us, is illegal and impracticable, and that any attempt to consolidate these roads and the Salt Lake Western should be abandoned. The committee presents a new plan, showing the amount of each class of new securities and the allotments to present creditors on the basis of the earnings formula, adjusted to eliminate the Salt Lake and the cut-off. The plan provides that the lease of the Salt Lake Western and the trackage agreement between the Salt Lake and the Denver be disaffirmed and rejected

as of November 1, 1935. It is stated that no serious consideration need be given to any substantial claim which may arise from such disaffirmance and rejection, since the assets and prospects of the Denver do not permit any recognition of the claims of general creditors unsecured by lien.

The committee now suggests that normally, under principles applicable in the marshaling of assets, the Finance Corporation would be merely a general creditor and should not be permitted to participate in the reorganization or even to foreclose on Denver securities held as collateral, except to the extent that the part of the pledged collateral in which other creditors have no interest may prove insufficient to satisfy the claim. The stocks of the Salt Lake and the Salt Lake Western are regarded by the committee as such part of the collateral in which other creditors have no interest, and the testimony of the Finance Corporation's witness is cited to show that the loan is fully secured by these stocks. But, should this part of the collateral prove insufficient, the committee evidently recognizes the right of the Finance Corporation to receive the securities of the new company allocable in respect of the debtor's bonds pledged with the Finance Corporation, on the same basis as the other holders of like bonds. The plan in fact shows specific amounts of new bonds and stocks issuable against the pledged securities (other than the aforesaid stocks and the motor companies' stocks); likewise new securities issuable against the bonds pledged with the Railroad Credit Corporation and the Chase National Bank, and all such new securities are included in the suggested new capitalization of the Denver.

While the committee states that the new corporate management of the Denver would be free to take any steps that it may deem proper for the acquisition of the Salt Lake and the Salt Lake Western, and that there is no intention to obstruct an ultimate unification of all the properties, the committee asserts that we have no authority to alter the rights or impair the priority of any prime mortgage liens on the properties of the Denver or the Junction for the sole purpose of effecting a consolidation, as we allegedly attempt to do under our approved plan. The committee refers to the fact that a consolidation can be effected only by voluntary agreement of the interested parties. Its position is that its original plan accorded treatment to the Denver's bondholders in accordance with their relative priorities, and that such plan would be acceptable to the bondholders and the Finance Corporation, whereas under the plan approved by us the capitalization of the new company, the amount of fixed charges permitted, and the treatment of the Finance Corporation are unfair and inequitable, making the plan

impossible of acceptance. The committee evidences its active opposition and believes that such opposition will be general and that the plan is therefore impracticable and if certified to the court will cause extended litigation, expense, and delay.

Several interveners agree with the committee's proposal in principal, including the Chase National Bank, trustee of the debtor's refunding and improvement mortgage. The bank, in its capacity as mortgage trustee, did not file a petition requesting modification of the approved plan, but filed an answer to the committee's petition and a brief in which the structure of the committee's plan was analyzed and various modifications suggested, such as the allowance of some form of arbitrary to the cut-off representing a fair division of rates as between separate railroads. No party accepts the committee's proposed allotment of securities.

We wish to point out that the committee has no ground for an assumption that we would approve, in any event, a plan and a new capital structure such as the committee has promulgated for the Denver alone. Both of the plans presented for our approval contemplated the consolidation provided for in the plan approved by us, although on different terms. All parties to the proceeding supported such consolidation, and the record before us was made in contemplation of such an arrangement. We are not prepared to say that the capitalization which we might consider proper on this new basis would permit substantially better treatment of the Denver's bondholders than does the plan approved on the basis of a consolidation of all the properties.

It would seem that a disruption of the present intercompany agreements and an indefinite postponement of the benefits of unified operation and management should be considered in connection with the bondholders' ultimate interest. Consideration should also be given to the amount and probable value of the Salt Lake and Salt Lake Western stocks, together with the various new securities, which the committee now proposes to assign to the Finance Corporation for its claim of approximately $12,000,000. The committee and other interveners complain that under our plan the bondholders would pay too high a price for the effectuation of consolidation, but the proposed modified treatment of the Finance Corporation, with its implication that the debtor may lose its equity in the stocks of the Salt Lake and Salt Lake Western, can hardly be regarded as a desirable part of the committee's plan from the standpoint of the present bondholders.

In our prior report we stated that a consolidation of the Denver, the Salt Lake Western, the Salt Lake, the Junction, and the Goshen Valley would be in accord with our findings in *Consolidation of*

Railroads, 159 I. C. C. 522, and that it would eliminate unnecessary separate corporations and would effect operating economies. We found that such consolidation would be in the public interest and that it should be effected in connection with the plan, notwithstanding the facts that the Salt Lake, the Junction, and the Goshen Valley are not in trusteeship and that none of the corporations has sought consolidation under section 5 (4) of the Interstate Commerce Act, as amended.

The Moffat Tunnel Commission and the Tunnel District point out in their reply brief that the tunnel project was associated with the policy of the Denver to establish a new short route between Denver and Salt Lake City, that the Salt Lake became the lessee of the tunnel, and that we authorized the building of the cut-off (*Denver & S. L. W. R. Co. Construction*, 154 I. C. C. 51 and 175 I. C. C. 535) and the acquisition of control of the Salt Lake by the Denver (*Denver & S. L. Ry. Co. Control*, 170 I. C. C. 4 and 175 I. C. C. 542). A loan from the Finance Corporation for the purpose of constructing the cut-off was approved by division 4 in *Denver & R. G. W. R. Co. Reconstruction Loan*, 187 I. C. C. 399, and a loan for the purchase of the Salt Lake's stock was approved by division 4 in *Denver & S. L. W. R. Co. Reconstruction Loan*, 202 I. C. C. 489. The terms of the trackage agreement by which the Denver operates over the Salt Lake were approved in 175 I. C. C. 535, *supra*. Under this arrangement one-half of the tunnel rental is paid by the Denver. Our approval of the present relationships of the Denver, the Salt Lake, and the Salt Lake Western was predicated throughout on considerations of public interest. In particular, our finding that the public convenience and necessity required the construction of the cut-off was based upon the making of an arrangement whereby the Denver could operate on fair and equitable terms over the cut-off and the Salt Lake, thus avoiding operation of the cut-off by the Salt Lake more or less in competition with the Denver's own route into Denver. After extended negotiations this arrangement was effected. Clearly the group's modified plan, which would jeopardize the continued unified operation of these properties, is inconsistent with our heretofore-expressed policy with respect to such operation.

To upset the present financial and operating arrangements, affecting all the affiliated carriers, as well as the Moffat tunnel interests, would clearly tend to undo much of what has been accomplished towards unification. It would, in our opinion, further complicate the present difficult situation and cause great delay in the permanent improvement of the conditions under which this through route is operated. It raises the question of good faith to

the Finance Corporation, whose loans were not made in contemplation of separate operation of the properties, notwithstanding the showing of independent value for the Salt Lake. Also, to continue the present lease arrangement, if the Denver were reorganized without a consolidation, would be unacceptable to the principal interests involved and would likewise postpone the desired unification. Consolidation appears to be inevitable, and it is desirable that the necessary adjustments of the classes of creditors accompanying the reorganization of the Denver, and the consolidation, be worked out as a single transaction.

While we recognize the fact that the acceptance of the plan in the manner provided in section 77 (e) is a prerequisite to the voluntary acts necessary to effect a consolidation of the Salt Lake with the Denver, as it is to the effectuation of the plan as a whole, our first duty is to promulgate a plan which we consider both financially sound and compatible with the public interest, and we reaffirm the finding that the properties should be consolidated in connection with this reorganization.

In addition to describing its new plan for a reorganization without consolidation, the committee presented a complete draft of the provisions for the new mortgages, bonds, stock, capital fund, etc., differing both from those originally advocated by the committee and from those adopted by us.

As has been stated, the view is advanced by several interveners that the consolidation of properties proposed to be accomplished under our approved plan would be at the expense of an unduly liberal treatment of the Finance Corporation, to the injury of the Denver's bondholders. The plan provided that the Finance Corporation should receive new first-mortgage bonds in an amount equal to its principal claim, plus interest accrued to June 30, 1938, a total of $11,959,469, conditioned upon a commitment by the Finance Corporation to purchase, at par, approximately $11,443,675 of the same series of bonds, the proceeds to be used for the purpose of redeeming $11,234,000 of Salt Lake bonds outstanding, and further to purchase approximately $6,000,000 of additional bonds for the purpose of paying the debtor's trustees' certificates outstanding, the expenses of the reorganization, and for working capital. We stated that the new first-mortgage bonds probably would not be salable at par and that the Finance Corporation should be compensated in some manner for its acceptance of them at par in return for furnishing the $17,443,675 of cash necessary to carry out the plan, but that such compensation should not be limited to the probable present deficiency in the market value of

the bonds. We pointed out that from 6 months to a year probably will elapse after the Finance Corporation makes its commitment before it will be called upon to supply the funds mentioned.

The plan provides that the Finance Corporation is to receive first-mortgage bonds in settlement of its claim while the holders of the R. G. Western first trusts and the Junction first-mortgage bonds are assigned income bonds, although, according to the earnings formula, the interest requirements on these three classes of obligations are fully covered. The basis for the allotting of first-mortgage bonds to the Finance Corporation is furnished, as has been indicated, by the consideration that the Finance Corporation will advance $17,443,675 in cash, for a like amount of the new first-mortgage bonds in order that the reorganization and consolidation may be effected. The new first-mortgage bonds may not be marketable when issued at a price much above 75, in which case the Finance Corporation should be compensated in some form for a service in effect costing approximately $4,400,000. That the allotment of first-mortgage bonds in lieu of income bonds is not unduly compensatory seems evident when the probable difference in realizable value between the two classes of new bonds is considered. In our opinion the differential between their initial market prices will not exceed 30 points, or about $4,000,000 for the $11,959,469 of bonds, representing the probable maximum amount of the concession made to the Finance Corporation in respect of the qualitative treatment accorded to it. While only approximate estimates can be made in this connection, we think that our provision for the Finance Corporation is entirely justified by the circumstances. In the matter of the collateral security for the loans, we think that the element of strategic value in the stocks of the Salt Lake and Salt Lake Western is such as to outweigh any question of inadequacy of collateral on an ordinary appraisal basis.

The debtor requests us to approve the plan originally presented by it, or at least to modify our approved plan so as to provide for two classes of new common stock, to exclude interest accrued but unearned since the filing of the petition, under section 77, to increase the amount of new first-mortgage bonds issued in the reorganization, and to recognize an equity for the present stockholders. The trustee of the R. G. Western first-trust mortgage and the Junction first-mortgage contend that these mortgages should be left undisturbed and the bonds extended, or, in the alternative, that these bonds be treated not less favorably than the committee proposes in its position, or that we refuse to approve any plan at this time. The trustee of the D. & R. G. consolidated mortgage requests that we modify the plan by allotting to the holders of the

consolidated-mortgage bonds new first-mortgage bonds to an extent commensurate with the value of the mortgage property, such bonds to bear interest corresponding to the earnings of that property. The trustee of the R. G. Western consolidated mortgage urges the adoption of a 2-percent interest rate for the use of equipment, an assignment of certain equipment to the liens of the mortgages in a manner differing from that reflected in our plan, and a different disposition of the stock of the Utah Fuel Company. The trustee of the debtor's general mortgage asserts, among other things, that the holders of general-mortgage bonds should receive 1 share of new common stock for each $100 of claim, including fixed interest accrued to December 31, 1939 (18 months later than the effective date of the plan), together with one-half share for each $100 of contingent interest accrued between February 1, 1924, and February 1, 1929, making a total of 430,974 shares of new common stock, as compared with 123,786 shares allotted to these bondholders in the plan.

The Chase National Bank of the City of New York, as noteholder, contends that the 10-year extension of its note, subject to renewal at the option of the new company, for further periods of 10 years each, as provided in the approved plan, is inequitable, and, inasmuch as the present note is a demand note and became due and payable when the petition under section 77 was filed, the renewal should be for 10 years only. The trustee of the Missouri Pacific Railroad Company urges that our plan provide for the retention by that carrier of its half interest in the Denver, as a matter of public interest, regardless of the existence of any equity for the Denver's present stock. The trustee also questions our provision that the new preferred stock shall have voting rights, since the present preferred is without such rights, and suggests that either the new preferred should not have voting rights equal to the common or it should be permitted to elect only a minority of the board of directors. The Security Research Bureau suggests numerous revisions of our plan, including an increase in fixed charges, the addition of a prior-preferred stock, changes in the mortgage and stock provisions, changes in the formula calculations and the allotment of new securities, and a different treatment of the claims of the Finance Corporation. The petitioners criticized practically every feature of the plan. We shall not undertake here to review in detail the contentions made with respect to the various points at issue, nearly all of which were discussed in our prior report.

After consideration of the petitions, briefs, and reply briefs filed, we conclude that the proceeding should not be reopened for further hearing or oral argument, that the suggested reorganization with-

out consolidation would be inconsistent with the record made herein and contrary to the public interest, and that as to all essential matters the petitions should be denied.

From a reconsideration of our prior report and order, we are of the opinion that certain provisions of the plan should be modified and certain other provisions, as to which some question has been raised, should be retained without change. These matters are discussed below and our conclusions are stated.

New First Mortgage

1. In the plan formerly approved it was provided that the interest on the first-mortgage bonds issued in the reorganization should be payable annually. In order to conform with usual practice and to enhance the marketability of the bonds, we conclude that this provision should be revised so that the fixed interest shall be payable semiannually.

2. Our plan provided that no additional first-mortgage bonds should be issuable unless the income of the new company available for fixed charges in a period of 12 consecutive calendar months within the preceding 18 calendar months equals or exceeds 1½ times fixed charges. Believing that this requirement is unduly restrictive and in general ineffective, we conclude that the provision should be omitted in the plan. See *Chicago, M., St. P. & P. R. Co. Reorganization*, 239 I. C. C. 485.

3. The provision for a special sinking fund for the retiral of first-mortgage bonds when the amount of fixed-interest debt exceeds a certain percent of total capitalization is retained. Those provisions would be effective when the total principal amount of fixed-interest-bearing securities exceeds 35 percent of the total capitalization, or 50 percent of the total capitalization less the amount of contingent-interest-bearing debt. The committee asks that these two percentages be increased to 50 and 60, respectively. Under the capitalization and initial debt provided for in our plan, the second of these criteria would, within all practical limits, constitute the limitation on the issue of new fixed debt as long as the contingent-interest debt remains the same. The criterion of 50 percent proposed by the committee would be ineffective under such circumstances. In our opinion the 35 percent approved by us should not be modified.

It appears that the second criterion approved by us is susceptible of two interpretations, and under one interpretation would force the immediate use of the sinking fund. The 60-percent limitation proposed by the committee would, under this interpretation, per-

mit the issue of approximately $30,000,000 of first-mortgage bonds, and we approve that limitation.

In order to avoid possible ambiguity in the language of our former report and also to make the above-indicated adjustment, the following is approved as a modification of the opening sentence of the provision in question:

(2) When on any interest payment date the aggregate principal amount of first mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either 35 percent of total capitalization, as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding, the new company shall pay to the mortgage trustee as a sinking fund a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, the payment to the capital fund, contingent interest, and sinking fund payments for the retirement of income bonds as hereinafter prescribed.

No further changes in the provision for this sinking fund are necessary.

4. The following additional provision regarding the pledging of first-mortgage bonds as collateral is approved:

The first mortgage shall contain a covenant substantially to the effect that the excess of the aggregate amount of all first-mortgage bonds under pledge at any one time, over the principal amount of all indebtedness so secured, shall not exceed 10 percent of the aggregate principal amount of all first-mortgage bonds then authenticated and uncanceled.

5. The following provision, being superfluous, is deleted from the plan:

No sinking funds shall be provided for the new first-mortgage bonds (except in the case of bonds issued for equipment) other than as provided in (2) above.

New Income Mortgage

The following additional provision regarding the pledging of income bonds as collateral is approved:

The income mortgage shall contain a covenant substantially to the effect that the excess of the aggregate principal amount of all income-mortgage bonds under pledge at any one time over the principal amount of all indebtedness so secured shall not exceed 10 percent of the aggregate principal amount of all income-mortgage bonds then authenticated and uncanceled.

Application of Available Net Income

The following provision is approved as a substitute for paragraph 3 in the sequence in the approved plan describing the application of available net income, in order to give effect to the special sinking fund for the retiral of new first-mortgage bonds:

3. Any then remaining available net income shall be applied to payment to the sinking fund to be created and paid to the trustee under the first mortgage in the event the principal amount of first mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either (*a*) 35 percent of the total capitalization of the new company, determined as elsewhere provided in the plan, or (*b*) the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding.

New Preferred Stock

The meaning of the closing sentence of the provisions for the new preferred stock being questioned, we approve the following in lieu thereof:

The new preferred stock shall be convertible at the option of the holder at any time, except that stock which is called for redemption shall be convertible not later than 15 days prior to the date as of which such call shall be made, into new common stock at the rate of one share of common stock for each share of preferred stock.

Chase National Bank Note

We approve a revision of the provision for extending the debtor's obligation to this bank so that the new note or notes shall mature in 10 years, without an option to the new company to extend the note or notes. The opening sentence of our provisions for the note will be modified to read as follows:

The secured note held by the Chase National Bank shall be canceled, and a new note or notes issued in face amount equal to that of the present note, plus interest accrued to June 30, 1938, in the amount allowed by the court, such notes to mature in 10 years and to bear interest at the rate of 4 percent per annum, payable semi-annually on October 1 and April 1 of each year, but such interest shall be contingent on, and payment thereof shall be limited to, the total of the interest and dividends paid by the new company on the collateral securing such notes.

No further changes in the provisions for this bank note are approved.

In the summary of the approved plan, 233 I. C. C. 515, 593, the annual interest on the extended note was shown as a fixed interest charge. In the revised summary of plan, shown later herein, such interest is included as a contingent charge.

Adjustment of Amounts of Claims

The adoption of the following new provision in the plan is approved:

In view of possible changes in the amounts of the obligations shown as outstanding, the reorganization committee shall be authorized, in order to give

effect to such changes, to make such adjustments in the claims provided for in the plan, and such changes in allotment of securities, consistent with the provisions of the plan, as may be approved by the court.

Voting Trust

Our prior report and order provided for the creation of a voting trust for the new common stock for the primary purpose, as explained in the report, of permitting a sale of control to the present proprietary companies or others, as the stockholders might decide, the terms and conditions of such sale to be subject to our approval. Upon further consideration we deem it desirable that both the new preferred and the new common stock be deposited under the escrow agreement, since the two classes of new stock are to have the same voting rights. With this modification and a provision for the compensation and expenses of the trustees, the approved provisions for the voting trust will read in full as follows:

K. All the preferred stock and common stock issued by the new company in the reorganization, excepting shares issued to qualify directors, shall be deposited under an escrow agreement with a bank or trust company designated by the court, and escrow receipts issued to the persons entitled to receive such stock under the plan. The escrow agreement shall be for a term of 10 years from the date of creation of the trust, but not later than 6 months after confirmation of the plan, and shall provide that the reorganization committee, as voting trustees, may, subject to the approval of this Commission, and with the consent of the holders of escrow receipts representing not less than a majority of the shares of preferred stock on deposit, sell all or any part of such deposited preferred stock at such price or prices as they may deem advantageous to the interest of the new company and its stockholders; likewise the voting trustees may sell all or any part of the deposited common stock with the consent of the holders of escrow receipts representing not less than a majority of the shares of common stock on deposit. It shall be provided that all holders of escrow receipts shall be bound by the terms of any sale or sales which shall have been approved by this Commission and consented to as aforesaid, and the net proceeds of any sale or sales, together with any unsold stock, shall be distributed pro rata among the holders of the escrow receipts for preferred stock and common stock, respectively, according to the class of stock sold. During the life of the escrow agreement, the holders of escrow receipts shall have the right to receive notice of all meetings of stockholders and to direct the voting trustees as to the manner in which the stock represented by the escrow receipts shall be voted at such meetings. In the absence of such directions, the deposited stock shall be voted in such manner as the voting trustees may determine. The reasonable compensation and expenses of the voting trustees, including counsel fees, shall be paid by the new company.

Unsecured Claims

The record showed that the amount of general unsecured claims outstanding was approximately $440,000, of which an undetermined amount fell within the 6-month rule. The unpledged securi-

ties owned by the debtor and its subsidiaries having a realizable value consisted of $46,000 of certificates issued by the receiver of the Rio Grande Southern Railroad Company and $850,000 of United States Treasury bonds. The latter have passed out of the debtor's possession. The present value of the receiver's certificates is uncertain, but in any event any distribution of new stock based upon this free asset, among the holders of the general claims and among the holders of the general-mortgage bonds in recognition of claims which they might present based upon the allotment of new common stock under our plan, would obviously be insignificant in amount. We conclude that the equity of the holders of unsecured claims not entitled to priority is without value and that these creditors should not be permitted to participate in the plan. Our modified order will accordingly omit provision for the general unsecured claims.

Reorganization Committee

Our plan provided for a reorganization committee to consist of five members, two to be designated by the insurance-group committee, as representing the R. G. Western mortgages, the Junction first mortgage, and the D. & R. G. consolidated mortgage, one member to be designated by the trustee under the debtor's refunding and improvement mortgage, one by the trustee under the debtor's mortgage, and one by the Finance Corporation. Further consideration of the composition of the committee has not resulted in any change in our views regarding it. Under our plan the Finance Corporation will have a large interest in the new company, and we think that it is clearly entitled to representation on the committee.

The two following revisions of the provisions for this committee are approved:

[new] Should any of the parties named fail to designate its representative or representatives, as the case may be, within such time as the court shall consider reasonable, the court shall appoint such representative or representatives.

[modified] The members of the committee, as such, shall agree to serve without compensation, but the expenses of the committee shall be paid by the new company, subject to the provisions of section 77 and the approval of the court, as part of the cost of effectuation of the plan. In their capacity as voting trustees the members of the committee shall be entitled to compensation and expenses as provided above in connection with the voting trust.

* * * * * *

Allocation of new securities under plan disapproved by the court omitted here.

We conclude that except as herein indicated the requests for modification of the plan of July 11, 1939, should be denied. An appropriate order will be entered accordingly, in which, with the foregoing modifications, our former plan will be approved. Such order will supersede the order of July 11, 1939.

EASTMAN, *Chairman*, concurring in part:

The essential purpose of the bankruptcy proceeding is to protect the interests of the creditors of the Denver, and the reorganization plan ought to make the best possible provision for them that the circumstances will permit. I am not wholly persuaded that consolidation of the Denver with the Salt Lake and the Salt Lake Western on the terms proposed will accomplish this result. It seems to be assumed that large benefits will accrue to the Denver from such a consolidation and that these benefits will be lost if the properties should become independent in ownership and operation. It is not clear to me that this assumption is correct, and I should be glad to hear argument on the point.

As between the Denver and the Salt Lake, my impression is that the Denver has the advantage in strategic position. The connection between the two railroads via the Dotsero cut-off is of value to both, but it would seem that it is more valuable to the Salt Lake than to the Denver. The latter now constitutes the only outlet of the Salt Lake to the west, but the Salt Lake does not constitute the only outlet of the Denver to the east. It has quite a good outlet for most eastern traffic via Pueblo and the Missouri Pacific. If the Salt Lake and the Salt Lake Western were independently owned, it seems to me that the Denver could safely rely upon this strategic position for assurance that favorable traffic and operating arrangements via the cut-off route could readily be made, and that the possibility of a unification of the roads on terms fully as favorable as, and probably more favorable than, those now proposed would not at all be foreclosed. This assurance would be strengthened by the natural interest of the Burlington, and to some extent of the Rock Island, in the development of the cut-off route.

Much is said in the report about our prior approval of the present relationships of the Denver, the Salt Lake, and the Salt Lake Western, and about "good faith to the Finance Corporation, whose loans were not made in contemplation of separate operation of the properties." As it happens, I did not join in the approval of acquisition by the Denver of stock control of the Salt Lake at the price of $155 per share, and believe that this transaction was harmful rather than helpful to the Denver; but, however that may be, the interests of the creditors of the Denver are paramount in the pres-

ent proceeding, if I understand the law correctly. And it seems to me that the Finance Corporation, when it made the loans in question, assumed the customary risks of such transactions.

I record these impressions for what they may be worth. It may be that they are wrong, but as at present advised I cannot join in what is said in the report with respect to the consolidation of these properties.

COMMISSIONERS MAHAFFIE and PATTERSON did not participate in the disposition of this case.

* * * * * *

Text of plan disapproved by the court omitted here.

INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

Submitted March 5, 1942. Decided July 13, 1942

Upon record previously made, the record made in proceedings before the court, and further hearing, the plan of reorganization for the Denver & Rio Grande Western Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, further modified and approved.[1]

Appearances as in prior reports, and also *Montgomery Dorsey, William J. Kane, Emmet McCaffery, Russell L. Snodgrass, Guy M. Springer, Jr.*, and *W. Brua Campbell.*

Second Supplemental Report of the Commission

BY THE COMMISSION:

Exceptions to the examiner's second proposed report were filed, and oral argument was heard. Our conclusions differ from those of the examiner.

The abbreviated titles of companies used in our prior reports will be followed herein. The insurance group committee will be referred to as the committee, and the Reconstruction Finance Corporation as the Finance Corporation.

Status of the proceedings.—By our report and order of July 11, 1939, in this proceeding, 233 I. C. C. 515, we approved a plan of reorganization of the debtor and the secondary debtor, and by a supplemental report and order, dated April 2, 1940, 239 I. C. C. 583, we approved a modified plan. The modified plan was duly certified to the District Court of the United States for the District of Colorado, where the proceedings for reorganization are pending. Pursuant to an order of that court entered May 6, 1940, objections to the plan were filed with the court by the debtor, the committee, the Finance Corporation, and other parties, and the case came on for hearing on July 29, 1940. Following an informal conference

[1] Previous reports: 212 I. C. C. 105 and 709; 217 I. C. C. 101; 224 I. C. C. 574; 233 I. C. C. 515; 239 I. C. C. 583; and 242 I. C. C. 529 and 721.

with the parties after the close of the hearing, the judge issued an interim memorandum, dated August 30, 1940, in which he expressed his views regarding the main features of the plan. Further conferences were held; and a new plan, proposed by the committee and known as the discussion plan, was considered. On December 6, 1940, the judge filed an opinion in which he criticized the discussion plan and our modified plan, and suggested a different plan.

The adoption of the discussion plan was urged in a petition filed with the court by the Central Hanover Bank & Trust Company, trustee of the Rio Grande Western first-trust mortgage. On January 6–8, 1941, the court heard the parties in oral argument, after which several conferences were held. A plan referred to as the FitzGibbon plan was presented at these conferences. On March 7, 1941, the court entered an order overruling a motion to dismiss the proceedings, disapproving our modified plan, and referring the proceedings back to us, with an opinion dated March 6, 1941. In this opinion, the judge indicated his objections to the various plans offered, including a plan proposed by the Finance Corporation, and described a plan which he recommends, hereinafter referred to as the court plan. The record made in the court proceedings was transmitted to us, and has been considered by us as a part of the record in the proceedings.[2]

Upon petition by the committee, an order was entered reopening the proceeding and assigning it for further hearing on May 20, 1941, for the purpose of receiving evidence to bring the record of the debtor's operations down to date, and such other evidence and suggestions as would assist in a reconsideration of the plan. Briefs were filed. The briefs were devoted largely to criticisms of, and suggested changes in, the court plan. In connection with its exceptions to the examiner's second proposed report, the committee suggested various changes in the plan therein recommended, embodying such suggestions in the form of a new plan.

The court plan.—The court plan differs in essential respects from our modified plan of April 2, 1940, although intended to be within the framework of the latter. The court agreed with us regarding a consolidation of the lines, stating in its opinion that, "Consider-

[2] Section 77, subsection (c), provides in part as follows: "If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) hereof."

ing the public's point of view and that of all creditors, this particular situation requires a consolidation of the Rio Grande and the Denver & Salt Lake." But the court's provision for consolidation was that it would be effected only in the event the holders of at least 66⅔ percent of the Salt Lake income bonds voluntarily accept a modification of the interest provisions of these bonds so that they would bear fixed interest at 4 percent. The effective date of the court plan would be January 1, 1941, while that of our modified plan was June 30, 1938, involving an increase of approximately $15,000,000 in accrued interest on funded debt, together with new equipment obligations. The amount of new first-mortgage bonds would be increased from $29,403,144 of 4-percent bonds, as provided in our plan, to $41,120,142 of bonds bearing 3-percent fixed interest and 1-percent prior-contingent interest. The $1,278,539 of annual fixed charges in our plan would be increased to $1,887,552 under the court plan, principally by the inclusion of the Salt Lake bonds. The allocation of securities to others than the Finance Corporation was generally on the same percentage basis as in our plan, but, as a consequence of the increase in first-mortgage bonds and the different treatment of the claim of the Finance Corporation, the court's treatment of the Denver's bonds was much more favorable. The court plan provides that the payment to the capital fund, a maximum of $750,000 per annum, be made prior to the payment of fixed interest, rather than immediately following. For the new money required in the reorganization, the Finance Corporation was asked to purchase $6,000,000 of income bonds, which would be convertible as a unit into class B common stock, carrying sole voting power. The right of sale of this stock by the Finance Corporation, for its reimbursement, would be restricted so that no one of the connecting railroads could obtain more than 40 percent thereof.

In our report of April 2, 1940, *supra*, we reviewed the development of the cut-off route, the close affiliation between the component roads, the Moffat tunnel interest, and the question of public interest, and reaffirmed our previous finding that the properties should be consolidated in connection with this reorganization. We also pointed out the status of the Finance Corporation as pledgee of the stocks of the Salt Lake and Salt Lake Western, and stated our reasons for the treatment accorded the claims of the Finance Corporation. It appears that the court rejected our modified plan because, through this treatment of the Finance Corporation and the relative treatment of the debtor's bondholders, particularly those owning the bonds of the Rio Grande Western and the Junction, the price to be paid for consolidation was too high, and the

plan was deemed inequitable. It is apparent that in this important respect our former plan is impossible of approval or acceptance.

The most feasible means of effecting a consolidation of the Salt Lake now appears to be along the lines suggested by the court. As to the court's treatment of individual claims, we are unable to accept the view expressed by counsel for the committee, that the court plan constitutes an adjudication of the rights of the creditors and is now the law in the case. We do not think that the court intended to preclude us from preparing and approving a new plan, provided such new plan reflects the equitable principles laid down in its decision.[3] Full consideration has been given by us to the conclusions and suggestions of the court, and in the light of them and from our review of the evidence we have made the determinations as to the treatment of creditors, hereinafter set forth.

Debtor's position.—Despite our finding that the equities of the debtor's stockholders have no value, and the court's failure to find otherwise, the debtor still contends that an equity worth at least $40,000,000 exists, that no reorganization can be accomplished without a lawfully determined valuation of the property, and that the fairness of the court plan cannot be determined without such valuation. However, various specific objections to the court plan were offered, such as its recognition of interest accruals in excess of $7,000,000 since September 1, 1935, the treatment of the Finance Corporation, the provisions for sale of control, and the inclusion of the Junction, which is not a debtor under section 77. The debtor—

> reserves its objections to the proceedings going forward before the Commission or the court until a new plan or plans are filed, the feasibility thereof determined, and hearings thereon ordered in accordance with subsection (d) of section 77 of the Bankruptcy Act.

The debtor's general position with respect to the purpose and scope of section 77, and the rights of creditors and stockholders, was stated in 233 I. C. C. 515, *supra*, at pages 573 and 578, and requires no further comment. Since our previous decision in this case, the decision of the United States Supreme Court in the case of *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510, sup-

[3] In this connection the court said: "My three opinions in this matter, it is thought, set forth the reasons moving the Court to disapprove the ICC Plan and send it back to the Commission for further hearings and consideration. The Court recognizes the Commission is well versed and peculiarly fitted to appraise the values of different interests and the soundness and fairness of any plan. If it does not agree with the views of this Court, any new plan they submit is most likely to receive our approval. The rights of the parties have been so minutely explored and discussed that it is hoped there may be little difficulty in the parties reaching an agreement upon a plan that meets the views of the Commission and the Court which are now in the record."

ports the views expressed by us with respect to the treatment of accruals of interest, and our disposition of the rights of the stockholders.

The plan herein approved, for reasons which will be stated, differs materially from the court plan and from the plan previously approved by us. In our opinion, the procedural requirements of section 77 have been and are being followed by our action in immediately hearing objections to the plan suggested by the court, without delaying the proceedings 6 months or more pending the filing of new plans for our consideration. We hereinafter specifically find the value of the properties for the purposes of this proceeding.

Consolidation of the properties.—The modified plan herein approved provides for the merger or consolidation of the properties of the debtor, the secondary debtor, the Junction, the Goshen Valley, and the Salt Lake; that of the secondary debtor to take place only if the Salt Lake is merged or consolidated, which would be subject to acceptance by the holders of the Salt Lake income bonds of the proposal for modification of the interest terms and maturity thereof, as hereinafter described. The manner of effecting such merger or consolidation should be determined by the reorganization committee, subject to approval by the court, and under a fair and equitable arrangement to protect the interest of the railroad employees affected, as required by law.

The present plan specifies the treatment accorded to each class of claims on the basis of consolidation with the Salt Lake, with appropriate provisions for the claims in the event such consolidation is not accomplished. If the consolidation becomes effective, the contract for use of the Moffat tunnel should be assumed by the new company, the holders of Salt Lake stock outstanding in the hands of the public should receive new securities in exchange therefor, and the payment of interest on both classes of Salt Lake bonds, modified so far as the income bonds are concerned, as provided in the plan, should be assumed by the new company, all as hereinafter set forth. The bonds of the new company should be secured by the combined properties of all the roads, subject to the prior liens of the Salt Lake mortgages with respect to the Salt Lake properties.

In the event the holders of the required percent of Salt Lake income bonds do not assent to the proposed modification of their bonds, and the consolidation thereby fails, the separate operation of the Salt Lake would continue and the stock outstanding, as well as the first-mortgage bonds and income bonds, would remain un-

disturbed. In this situation, the mortgage bonds of the new company would be secured by the properties of the debtor, the Junction, and the Goshen Valley only.

In neither event would the Salt Lake bonds be affected as to their liens.

Earnings; equity.—In our report, 233 I. C. C. 515, *supra*, at pages 551–552, we discussed the earnings record of the carriers, and showed that the lowest system income available for interest in the last decade was in the 3-year period 1936–38. After adjustment for extraordinary expenditures for deferred maintenance, the average annual income available was stated at about $2,893,255. The total of the fixed-interest charges approved under our modified plan and the maximum annual payment to the capital fund was approximately $2,098,536, which would have been covered 1.38 times by the foregoing amount of adjusted income. We stated, at page 552, that:

> In giving this consideration to the low earnings of recent years our position is not that the system lines will never regain their former earning power, or exceed it, but rather that, with the present conditions in the railroad field and in the public interest, a conservative policy should be followed * * *.

The evidence adduced at the further hearing shows that the improvement program has been substantially completed. From the appointment of the debtor's trustees on November 1, 1935, to March 31, 1941, a total of $22,916,051 was expended on the debtor's property, of which $17,504,246 was chargeable to capital account. The ratios of maintenance to total revenues had been 35.12 in 1935, 41.09 in 1936, 46.83 in 1937, and 39.09 in 1938. The debtor believes that the improvements already made, together with the acquisition of new Diesel switch engines and road engines costing $4,000,000, will produce a large and permanent reduction in operating costs. The results of operation in 1940 are considered by the committee to be fairly representative as to economy of operation as well as to gross revenue, based on 5 years of the trusteeship. The income of the Denver available for interest in 1940 was shown as $2,800,514[4] and the Salt Lake's available income as $509,771, a total of $3,310,285. Previous totals were $2,299,867 in 1939, $673,358 in 1938, $295,504 in 1937, and $2,327,757 in 1936. The committee pointed out that, applying the unit costs of operation in 1940, the available income of the combined roads would have been $3,288,501 in 1939, $2,970,135 in 1938, $3,774,334 in 1937, and $3,890,570 in 1936. The average for the 5 years would have been $3,446,765. These

[4] Adjusted from the amount of $2,647,086 shown in the 1940 annual report of the Denver's trustees to the stockholders.

figures reflect operating charges of approximately $1,000,000 a year in connection with improvements. The forecast for 1941 indicated an available income of $3,513,590 for the combined roads, and the actual amount was $5,019,436.

We cannot, of course, accept the committee's adjusted figures as expressing what the company's earnings would have been under improved conditions in the stated years. The earnings in 1940 and 1941 indicate an improvement in the earning power of the system, but do not justify a modification of our findings regarding the equity of the Denver's stockholders (233 I. C. C. 515, at page 580) or of the holders of unsecured claims (239 I. C. C. 583, at page 594). The principal of the debt (including R. C. C. notes, R. F. C. notes, and trustees' certificates), of the Denver as of January 1, 1942, is $143,181,421, and annual interest charges thereon amount to $6,137,715. In addition, accrued and unpaid interest to January 1, 1942, on the Denver's debt amounts to approximately $42,499,558, and interest on this obligation at the rates applicable to the principal obligations would require an additional $1,944,555. The claim on this unpaid interest must also be provided for before the junior claims and the stock can receive anything. Interest upon the principal and unpaid interest of the Denver's debt at 4 percent is $7,427,239 and at 5 percent is $9,284,049. Both amounts exceed the above-stated income available for interest in either 1940 or 1941 for the Denver or the Denver and the Salt Lake combined. Income of the Denver and the Salt Lake available for interest in 1940 capitalized at 4 percent is $82,757,125, and capitalized at 5 percent is $66,205,700, and the above-stated system earnings for 1941 similarly capitalized are $125,485,900 and $100,388,720, respectively. Each of these amounts is less than the principal amount of the Denver's debt. We reaffirm our findings that the equities of the owners of the debtor's common stock and preferred stock have no value and that the holders of claims in classes 1 and 2 are not entitled to participate in the plan; and that the equity of the holders of unsecured claims not entitled to priority is without value and that these creditors should not be permitted to participate in the plan.

New capital structure, fixed charges.—Under the court plan, the total capitalization of the new consolidated company, taking the common stock at $100 a share, would be $161,611,891, the total debt would be $90,411,051, and the total charges before dividends $4,569,644. Fixed charges would amount to $1,887,552 per annum, without the capital fund, and $2,637,552 per annum, including the payment of $750,000 to the capital fund, which the court placed

ahead of all fixed interest. There would be a further increase of $411,201 if the court plan were modified as suggested by the committee so as to make the prior contingent interest on the new first-mortgage bonds a fixed charge in the event all fixed and prior contingent interest should be earned 1½ times in each of 3 calendar years in any 5 consecutive years, such 3 years to include the last 2 of each 5 years. The court had before it, in addition to the record made before us, the results of operation for the years 1939 and 1940.

In determining the amount of fixed charges in connection with our former plan, we gave consideration, as above stated, to the carriers' earnings record up to the close of 1938, including the low earnings during 1936–38 as actually reported, and as adjusted for deferred maintenance. The total amount of fixed-interest charges which we approved for the consolidated company was approximately $1,278,539, not including the capital-fund requirement. The development of the record at the further hearing before us led the examiner to recommend a limit of approximately $2,000,000. The total fixed-interest charges under the plan hereinafter approved are shown as $1,766,966, on the basis of the present equipment obligations and a consolidation of the properties.

The improvements recently completed on track and structures, together with the new acquisitions of equipment, will undoubtedly result in more efficient operation and reduced cost of maintenance. The committee concludes from its studies that the minimum future earning capacity of the combined properties is substantially in excess of $3,000,000 a year, and the court has expressed a similar opinion. In view of the record of the results of the debtor's past operations, as hereinbefore set out, the emphasis which the court has placed on measures to prevent future financial difficulties, and the uncertainty of future economic conditions in the country, and considering all of the facts of record with respect to the debtor's earning power, and all other relevant facts, we find that the total fixed-interest charges under the plan herein approved, on the basis of the present equipment obligations and a consolidation of the cut-off lines with the Denver, should not exceed approximately $1,766,966. Further, we believe that the plan should provide that payment of the fixed interest on the new first-mortgage bonds may be deferred, with the assent of the bondholders, under the conditions and in the manner hereinafter stated.

For the purpose of comparison with our former plan, the above amount plus the payment of $750,000 to the capital fund equals $2,516,966. This amount was covered 1.37 times by the average earnings during the period 1936–40, developed by the committee

on the basis of 1940 operation costs. Under the former plan, the corresponding charges were covered 1.38 times by the adjusted earnings of 1936–38. We find that, under the conditions imposed, the above charges will be adequately covered by the prospective earnings of the reorganized company.

Effective date.—The effective date of the plan recommended by the examiner, and shown in the modified plan suggested by the committee, was January 1, 1942, 1 year later than the date of the court plan. It is clear that a date later than that of the court plan should be adopted. We have considered the cash position of the debtor, its recent earnings record, the probable payments of interest and other probable disbursements by the trustees during 1942, and the cash requirements for interest payments and other payments, in order to carry out the plan herein approved. The system cash on hand January 1, 1942, amounted to $4,886,345, which, added to the cash receipts during 1942, as estimated from operations in the first 3 months, and giving effect to the proposed loan of $2,250,000 for new money, amounts to approximately $15,575,345. The total cash disbursements during 1942 under the plan would be approximately $12,231,000, including the payment of all outstanding trustees' certificates. The result of these estimates shows at least $3,344,000 of cash on hand at the close of the year. According to the testimony of the debtor's witnesses, this amount will be ample for cash working capital. Despite the increase in the total of present claims between January 1, 1941, and January 1, 1942, we conclude that the latter should be adopted as the effective date of the plan.

Capital fund.—We are reluctant to set aside the suggestion of the court that the payments into the capital fund be required or permitted prior to payment of fixed interest, but it seems desirable to avoid detracting from the future market value of the new first-mortgage bonds by appearing to provide for nonpayments of the fixed interest on them as a matter of course. Obviously, such a provision would be used or useful only if the earnings should be insufficient to make both the fixed-interest and the capital-fund payments. The virtual completion of the debtor's improvement program also tends to lessen the necessity for giving precedence to the capital-fund payments. The capital structure hereinafter approved by us is such that there are reasonable prospects in most years of making the capital-fund payments out of earnings, after payment of fixed-interest charges. We conclude that the payments into the capital fund should not be required or permitted prior to the payment of fixed interest.

Equipment fund.—The court also urged that the annual depreciation charge on equipment should be set aside in a special cash fund and used only to take care of interest and principal payments on equipment-trust obligations outstanding or issued later, and to take care of, in whole or in part, the purchase, building or improvement of equipment. The plan herein approved imposes strict limitations upon the reorganized company with respect to the use of its cash. The provisions of the mortgages prescribe the purposes for which all funds remaining after charges for operating expenses, including depreciation, may be used. At present, the maturities of the debtor's equipment obligations will require approximately 85 percent of the accruing depreciation reserve. This condition will continue for at least 7 or 8 years. In view of the foregoing, it is our view that we should not impose the suggested limitation of the use of the depreciation reserve.

Property valuations.—In our report, 233 I. C. C. 515, *supra*, at pages 521–523, we stated that the report of our Bureau of Valuation showed the cost of reproduction of the system properties, less depreciation, plus lands and rights, working capital, and net additions and betterments to December 31, 1936, as $147,717,268. If to this sum be added the net changes in investment accounts, reported in the carriers' annual reports for 1937 to 1940, inclusive, the total becomes approximately $155,900,000. A substantial addition to this sum will have been made during 1941, especially from acquisitions of equipment. On the basis of original cost, as also stated in 233 I. C. C. 515, *supra*, the total as of December 31, 1936, was $178,024,641. Adding the net changes in investment for the years 1937–40, this would become $186,207,418.

The securities representing investments of the debtor may be divided into four groups, as follows:

1. Those issued by subsidiary railroad companies which will be merged or consolidated with the debtor and whose operations have been taken into account in fixing the new capitalization. These securities will be canceled upon consummation of the plan, and no determination of their value is necessary, except in connection with the claim of the Finance Corporation, hereinafter discussed.

2. Securities (excluding $906,000 of Junction refunding bonds, which fall within the foregoing category) which are now pledged under the present refunding and improvement mortgage, in whole or in part, and which will be released upon consummation of the plan and presumably become subject to the lien of the new first mortgage. These securities consist of stocks of the following terminal companies in the par amounts indicated: $5,000 of stock of the Denver Union Terminal Company, $10,150 of stock of the

Pueblo Union Depot & Railroad Company, and $100,000 of stock of the Salt Lake City Union Depot & Railroad Company. The total book value of these stocks is $115,150. The income accounts of the three companies show deficits throughout from 1927 to 1936. These deficits are paid by the lessees of the terminals, and the Denver's portion is carried into its accounts as joint facility rents or other proper account. The operation of the terminal companies, therefore, is reflected in the distribution of net earnings.

3. Miscellaneous securities, some of which will be released from pledge upon consummation of the plan, and others of which are not under pledge, which presumably will be held as free assets by the new company. These comprise the Motorway stocks and the Rio Grande Southern bonds, all hereinafter considered in connection with the Finance Corporation claim, together with 5 shares of stock of the Railway Express Agency, $50,000, par value, of the stock of the Denver Market & Produce Terminal, and $2,801, par value, of the stocks of 12 small nonaffiliated companies. The total book value of the securities, other than the stocks and bonds pledged with the Finance Corporation, is about $95,000. We find that the free assets consisting of these securities have a value not exceeding the sum just stated.

4. The stock of the Utah Fuel Company, which is pledged under the Rio Grande Western consolidated mortgage, subject to the right of redemption. The evidence as to the value of this stock was reviewed in our report 233 I. C. C. 515, *supra*. The going-concern value of the property was appraised by a mining expert in 1937 at $4,653,720, which the trustee of the mortgage considers to be a conservative figure. The company's earnings are not of record since 1936, in which year, and in 1935, small amounts of net income were reported. The debtor, in its original earnings formula, credited the Rio Grande Western consolidated-mortgage district with an income of $83,333 a year from the fuel company. In the first plan presented by the committee, the allocation of new bonds to the claim of the Rio Grande Western consolidated included an allowance of $567,448 of income bonds for control of the fuel company. Since our plan provides that the beneficial interest in the stock shall be distributed pro rata to the bondholders, the matter will be discussed later in connection with the bondholders' claim.

New capitalization.—While the debt of the Denver has increased materially since the effective date of the former plan, there has also been an increase in earning power, as we have shown. Capitalized at 4 percent, the income of the system available for interest

in 1941 produces the sum of $125,485,900, and at 5 percent it produces $100,388,720. The trend of earnings indicates that in 1942 the debtors' forecast for a future normal year, showing an available income of $6,215,423, will be exceeded. That forecast of income capitalized at 4 percent would amount to $155,385,600, and at 5 percent, $124,308,500. Considering the entire record, and taking into account the elements of value of the properties involved, their past and present earnings and prospects for future earnings, as well as other pertinent factors, we conclude and find that the value of the properties for the purposes of this proceeding is $154,521,612, and that the total capitalization upon consummation of the plan should not exceed approximately that amount.

The new capital structure and the allocation of securities which we now approve, excluding securities to be pledged, are shown in tabulated form in appendix A, based on a general consolidation of the properties and the inclusion of the Salt Lake bonds, and in appendix B, without such consolidation with modification of the interest terms of the income bonds. Under this plan, the fixed charges would approximate $1,766,966, comprising $193,832 of interest on equipment obligations, interest at 3 percent on $36,120,366 of new first-mortgage bonds, interest at 4 percent on $1,500,000 of Salt Lake first-mortgage bonds, interest at 3 percent on $9,734,000 of Salt Lake income bonds (assuming all the holders consent to the modification of interest terms), and the estimated fixed interest payments on the Chase Bank note extended, the Railroad Credit Corporation note if extended, and a loan for new money in the amount of $2,250,000. Prior contingent-interest charges on the new first-mortgage bonds, the Salt Lake income bonds, and the new first-mortgage bonds to be pledged with the Chase Bank will amount to approximately $473,494. Contingent-interest charges on the $21,916,638 of new income bonds, and on the income bonds to be pledged with the Chase Bank (up to a total of 4 percent on the amount of the new note to be given the bank), will total approximately $1,009,185.

The total debt of the new consolidated company under this plan would be approximately $82,994,255, and the total capitalization would be approximately $154,521,612, including all equipment obligations. Total charges ahead of dividends on the preferred stock, including the maximum payment to the capital fund and the sinking funds, would be approximately $4,235,039, as compared with $4,093,842 in the plan formerly approved. This increase is justified on the basis of the earnings record, as supplemented at the further hearing. We find that the amount of the new company's obligations and the annual charges above stated may not be exceeded.

The capitalization last stated included $3,927,605 of obligations for equipment acquired in 1941, consisting of 17 Diesel locomotives and 5 Mallets, purchased under conditional-sale agreements totaling $2,667,605; and 500 boxcars acquired under equipment trust I for $1,260,000. The operating savings from this new equipment are not reflected in the unit costs in 1940, which were adopted by the committee as a criterion in adjusting the income accounts of 1935–39, and, on the theory that this new equipment will pay for itself by the economies which it will produce, the $3,927,605 of new equipment obligations might properly be considered as a separate item in the capital structure, in effect reducing the new total to $150,594,007. This figure would be comparable with the total capitalization of $147,433,350 under our former plan, taking the no-par common stock at $100 a share.

The effect of a reorganization of the Denver without consolidation of the Salt Lake would, under this plan, be to eliminate from the new capital structure the $11,234,000 of Salt Lake bonds, the $411,100 of new preferred stock allocated to the shares of Salt Lake stock outstanding in the hands of the public, and $1,000,000 of the loan for new money, hereinafter discussed. Also, instead of the new securities shown in appendix A as allotted to the Finance Corporation claim, other securities would be assigned for the system securities under pledge, and these, together with the remainder of the collateral, would be deposited in escrow for the benefit and interest of the Finance Corporation, subject to prescribed conditions, as hereinafter stated. On this basis, and with the Finance Corporation claim shown at its present amount, the total capitalization of the reorganized Denver would be substantially $141,876,512, the total debt $72,351,856, total fixed interest $1,765,973, and total charges before dividends $3,732,956.

Basis of allocation of new securities.—In our report in 233 I. C. C. 515, *supra*, at page 582, certain modifications of the debtor's segregation formula were introduced, for reasons stated, and the resulting distribution of income available for interest, based on the 12 months ended June 30, 1935, was as follows:

		Item
D. & R. G. W. operation:		
Own lines (88 percent)	$2,641,638	A
Cut-off (12 percent)	360,025	B
	3,001,663	C
Motorway, dividends	11,600	D
D. & S. L. operation	912,960	E
	3,926,223	

The amounts of items B, D, and E, totaling $1,284,585, were applicable to the claim of the Finance Corporation, subject to a deduction of $457,747 in respect of the Salt Lake bonds which were to be redeemed under the plan then approved.

The debtor's segregation study, as was explained in our report, reflected the actual earnings of the system during the 12 months stated, adjusted for intercompany charges, maintenance costs, the revenues from certain traffic, the savings from consolidation, and other factors, all with the purpose of providing a basis for the new capitalization and distribution of securities. The record contains no analysis of system earnings of a later period, developed in the same way. The actual earnings of the Denver from 1935 to 1940, inclusive, adjusted for deferred maintenance in 1935–38 on the basis used in our previous report, show an average available income of $2,316,016 a year, corresponding to the amount stated above as item C. As to the portion of this total income that was derived from the operation over the cut-off, B, the record shows that the ratio, of the overhead freight tonnage moving via Denver to the Denver's total freight, increased from 6.5 percent in 1935 to 9.1 percent in 1939. Thus the 12-percent proportion, reflected in the original study, should not have diminished materially. It is accordingly adopted in the present computation. The average dividends from the Motorway companies during the 1935–40 period were $13,956 a year, instead of $11,600 as shown in item D. The actual earnings of the Salt Lake averaged $566,908 a year, item E. Revised on this basis the formula would be as follows:

	Distribution of earnings			Item
	R. F. C.	Amount	Ratio	
			Percent	
R. G. Western first-trust 4's		$866,190	35.4	
R. G. Western consolidated 4's		—67,257	—2.7	
Junction first 5's		126,362	6.2	
D. & R. G. consolidated 4's and 4½'s		754,095	30.8	
Equipment trusts		101,904	4.2	
Refunding and improvement 5's and 6's		256,800	10.5	
Subtotal		2,038,094		A
Denver cut-off operation	$277,922			B
Subtotal		(2,316,016)		C
Motorway dividends	13,956			D
Salt Lake operation	566,908			E
R. F. C. claim	858,786			
Interest on Salt Lake bonds	[1]449,360			
Net for R. F. C.		409,426	16.7	
Total		2,447,520	100.0	

[1] Consisting of 4 percent interest on the Salt Lake first-mortgage bonds, and 3 percent fixed interest and 1 percent prior contingent interest on the Salt Lake income bonds, as contemplated under the plan hereinafter approved.

The amounts of first-mortgage bonds, income bonds, and stock available under the plan herein approved, distributed on the basis of these percents to the several bond groups (including separately the Denver's bonds pledged with the Finance Corporation) and to the claim of the Finance Corporation, would produce the following primary allocations:

	First-mortgage bonds	Income bonds	Preferred stock, $100 par value	Common stock, $100 par value
R. G. W. first trusts	$12,832,512	$6,610,688		
R. G. W. consolidateds		1,167,192	$13,422,708	$4,863,300
Junction firsts	1,754,509	903,833		
D. & R. G. consolidateds	11,108,669	6,876,795	11,637,653	23,275,307
Refunding and improvements	3,075,200	1,922,000	4,036,200	10,186,600
Finance Corporation	7,197,881	4,587,727	1,591,601	
Total	35,968,762	22,068,235	30,688,162	38,325,207

The above allocations to the Finance Corporation comprise the new securities applicable to the pledged bonds of classes publicly held, and the new securities directly assignable to the claim by the 16.7 percent in the formula.

Neither of the foregoing analyses reflect anything for the Finance Corporation's second lien upon the securities pledged under the notes held by the Railroad Credit Corporation and the Chase National Bank. On the basis of present liquidation value, it appears that this equity may have some value, although the amount cannot be definitely determined. It is our opinion that it is less than $300,000.

As compared with these allotments to the Finance Corporation, the court allotted $4,312,853 of first-mortgage bonds and $8,540,931 of income bonds, stating that the first-mortgage bonds were intended to equal the amount of the loan for constructing the Dotsero cut-off, with interest to January 1, 1941, the effective date of the court plan. (The correct amount as of that date was $4,820,480, and as of January 1, 1942, was $4,802,040.) The committee, analyzing the court plan and taking into consideration the pledged collateral of classes that are publicly held, asserts that the court allowed only $1,163,293 of first-mortgage bonds to represent the other collateral, consisting principally of the Salt Lake and Salt Lake Western stocks. That this was not the theory followed by the court is shown by the following statements in its opinion of March 6, 1941:

The Reconstruction Finance Corporation receives $4,312,853 in first mortgage bonds, which equals the amount of their so-called cut-off notes secured by Denver & Salt Lake Western stock. This stock, it must be remembered, is really a first mortgage on the cut-off, there being no bonds or other indebtedness ahead of it. On its old advances the Reconstruction Finance Corporation received $8,540,921 in income bonds, and in return is asked to purchase $6,000,000 more of 4½ percent income bonds for cash, to be used to pay the trustees' obligations and reorganization expenses. * * * The new company acquires the Salt Lake Western (the cut-off) from the Reconstruction Finance Corporation by the payment of the original cost thereof in first mortgage bonds.

The matter of the treatment to be accorded the Finance Corporation claim also may be approached from the standpoint of the securities allocable to the collateral under pledge with the Finance Corporation. This consists of the bonds, stocks, et cetera, enumerated in our report in 233 I. C. C. 515, at page 524, except for the changes in the amounts of Salt Lake and motor companies' stocks, the amounts of these securities on pledge now being Salt Lake stock, 45,889 shares; Denver-Colorado Springs-Pueblo Motor Way, 73,710 shares; and Rio Grande Motor Way, 1,748[*] shares. Under the percentage treatment of claims reflected in the allocations shown just above, the 4 blocks of Denver bonds under pledge would be entitled to $1,318,626 of new first-mortgage bonds, $701,619 of new income bonds, $2,720,286 of preferred stock, and $4,064,282 of common stock. The $1,266,000 of Salt Lake income bonds would be entitled to substantially a like amount of new first-mortgage bonds, since the fixed interest rate and prior contingent interest rate are made the same for both issues under the present plan. To represent the approximate value of the Motorway stocks, Rio Grande Southern bonds, and Goshen Valley stock, $250,000 of new first-mortgage bonds should be assigned; for the 45,889 shares of Salt Lake stock, an equal number of shares of new common stock; and for the 36,310 shares of Salt Lake Western stock, $1,815,500 of new first-mortgage bonds, $907,750 of preferred stock, and $907,750 of common stock. The total amount of new first-mortgage bonds thus arrived at is $4,650,126.

At the hearings before the court, the committee introduced evidence consisting chiefly of a severance study which purported to show that, for the year 1939, on the most favorable basis of computation for the Salt Lake, the Denver's income available for interest would have been increased by $323,451 if the Salt Lake and Salt Lake Western had been operated as a single independent road, interchanging traffic with the Denver at Dotsero; that the Denver had so far lost money by the cut-off operation; that the $391,000

[*] This amount was later increased to 1,858 shares. See *Denver & R. G. W. R. Co. Reconstruction Loan*, 252 I. C. C. ——.

of income of the Salt Lake available for interest in 1939 would have been converted into a deficit of $182,229 by the severance; that if all the roads had been operated as a consolidated system in 1939 the income available for interest would have been $2,512,184, while with the cut-off lines divorced it would have been $2,064,368. The conclusion was that something like $500,000 a year was the maximum realizable value of the Salt Lake-Salt Lake Western to the Denver.

The study depends upon several basic and important determinations, including the division of rates between the two carriers if operating independently, the amount of traffic moving over the cut-off in 1939 which could have been diverted via Pueblo, the additional cost of handling such diverted traffic, and the feasibility of handling the Denver's interchange with the Rock Island at Colorado Springs. These are highly controversial questions. It is noted that the study shows an increasing money benefit to the system by the inclusion of the Salt Lake, as the total revenues rise above those of 1939. While the Denver's interchange at Pueblo and Denver are both increasing, the largest increase, in terms of revenue and by individual roads, between 1937 and 1940, was with the Burlington at Denver.

The severance study purports to measure the value of the cut-off to the Denver or the consolidated system by calculating the effect of its separate and competitive operation, using a given amount of overhead cut-off traffic, and assuming that, by solicitation on the part of the Denver, the Missouri Pacific, and the Rock Island, approximately 64 percent of such traffic could be diverted to the Denver's own line via Pueblo. The benefit of the debtor from the portion of the haul west of Dotsero on traffic brought to the debtor by the cut-off is not separately reflected in the study as a credit to the cut-off.

The situation here is distinctly different from that existing in the Chicago & North Western Railway Company reorganization referred to by the committee which caused the judge to state that, since the Milwaukee, Sparta and North Western Railway Company was a "bridge line," the only fair measure of its value to the system was a severance study. *In re Chicago & N. W. Ry. Co.* (1940), 35 Fed. Supp. 230, 240. That opinion clearly states that the Sparta line was built for the purpose of reducing operating costs by diverting traffic from existing routes to the new bridge route. In the case now before us, the cut-off route was constructed to attract a larger share of transcontinental traffic to the debtor's line, and is considered as indispensable to the future of the debtor. Neither the segregation nor the severance studies reflect these factors. Any

real value in the cut-off arising from such factors is based on the ability of the debtor to solicit traffic routed over the shorter cut-off route and the extent that such solicitation is successful. Obviously, such traffic could not be routed through Pueblo, a fact which places a limitation upon the applicability of a severance study to the situation. Continued increase in traffic which must be routed over the cut-off would unquestionably render the severance study presented by the committee entirely inapplicable to the debtor's situation. We are not convinced that the full traffic possibilities of the cut-off as yet have been developed.

The narrow conclusions drawn by the committee from the severance study would encourage the view that a separation of the cut-off and the debtor into separate systems would benefit the debtor. Yet if such separation occurred so that there was competitive solicitation between the two routes, certainly if the study correctly reflects the situation, the result would be disadvantageous to the debtor to the extent that it forced routing of traffic over the cut-off. None of the studies reflects the effect of such competition or of such solicitation.

Such an analysis of existing traffic and earnings does not, in our opinion, adequately represent what the situation of the system would have been at the present time, or would be in the future, if the short route via Denver had not been created. The committee's witness estimated the amount of new business that was attracted to the cut-off in 1939 at some 195,000 tons, or 12.6 percent of all the overhead business. The committee's exhibits, however, show that the Denver's proportion of the combined transcontinental freight tonnage of the Denver and the Union Pacific (composing the so-called central group) increased from 21.2 percent in 1935 to 25.4 percent in 1939, and the Denver's proportion of the combined transcontinental freight tonnage of six important trunk lines increased from 6.0 percent to 7.4 percent. In the same period, the Denver's total overhead traffic increased from 1,058,512 tons to 1,551,341 tons, the amount moving via Denver increasing from 466,719 tons to 785,042 tons. It seems obvious that this favorable showing was due in large part to the existence of the cut-off route, although there was evidence that to some extent the increase was due to the opening up of other railroad facilities.

Notwithstanding the severance study, the judge expressed the opinion that the cut-off is "absolutely essential if the debtor is to have a future." The committee itself shows that, with a traffic increase of 10 percent over 1939, the estimated value of the cut-off, on a severance basis, expressed in earnings available for interest on funded debt, would rise to $685,929. The showing clearly fails

in providing a reliable figure to substitute in the formula for the earnings of the cut-off, that is, the proportion of total earnings to be assigned to the claim of the Finance Corporation. We are of the opinion that the formula distribution, modified to reflect the results of operation in the period 1935 to 1940, and otherwise, as explained above, is supported by the present record, and, although the results of the severance study may not be disregarded in this connection, they should not be accorded controlling weight.

Considering the foregoing, it is our view that, on the basis of the court's allotment of first-mortgage bonds, $4,802,040 of such bonds should be allotted to the claim of the Finance Corporation. In order to adhere as closely as possible to the formula, insofar as the distribution of debt securities is concerned, the excess of $2,395,841 of first-mortgage bonds would be distributed among the other claims entitled to receive first-mortgage bonds, in proportion to the respective earnings; the amounts of new income bonds allocable to those claims under the formula would be correspondingly reduced; and the amount of income bonds allocable to the Finance Corporation claim would be correspondingly increased. In terms of total new debt—first-mortgage bonds and income bonds—there would be no change, and the allotment of stock would not be affected. The adjusted distribution then would become:

	First mortgage bonds	Income bonds	Preferred stock, $100 par value	Common stock, $100 par value
R. G. W. first trusts	$13,804,672	$5,638,528		
R. G. W. consolidated		1,167,192	$13,422,708	$4,863,300
Junction firsts	1,887,416	770,917		
D. & R. G. consolidated	12,166,638	5,818,827	11,637,653	23,275,307
Refunding and improvements	3,459,600	1,537,600	4,036,200	10,186,600
General-mortgage bonds				2,102,888
Finance Corporation	4,802,040	6,983,568	1,591,601	
Total	36,120,366	21,916,632	30,688,162	40,428,095

Appendix C shows the development of the percentage allotments to the claims of the several bond groups, based upon the above table.

From a consideration of the foregoing analysis of the segregation study, the severance study, and the other matters referred to, we conclude that the distribution of securities to the various creditor classes should be as shown in appendix A of this report, based upon consolidation of all the properties, or as shown in appendix B in the absence of consolidation.

The individual claims will now be discussed.

Finance Corporation claim.—We have explained the basis adopted for the treatment of the Finance Corporation's claim in connection with the general distribution of new securities. The above assignment of new bonds and preferred stock, based as it is in part on the application of the cut-off arbitrary, reflects any strategic value there may be in control of the Salt Lake and Salt Lake Western now held by the Finance Corporation. This question, and the considerations pointing to the desirability of a general consolidation of the properties, were discussed at some length in our report on further consideration, 239 I. C. C. 583. While we are still of the opinion that the cut-off traffic possibilities have not yet been fully realized, it is our view and we find that, under present and prospective traffic conditions and on the evidence presented, it is impossible to find any value in the cut-off control in addition to that reflected in the allocations made above. In this situation, and in view of the fact that the Finance Corporation is not required to take any new securities in providing the new money needed in the reorganization, the plan will not provide for an issue of management stock to the Finance Corporation as was done in the court plan.

The Finance Corporation urges us to recognize and allow for the rental payable under the Salt Lake Western lease and supplemental agreements, which the debtor's trustees have not yet elected to affirm or disaffirm. A petition for the payment of this rental was filed with the court on March 25, 1936, by the trustee of the Salt Lake Western, but has never been acted upon. The Finance Corporation has been advised that the total amount due under the lease, as of January 1, 1942, was $1,179,666. The Finance Corporation contends that, if the payment of such sum to it, as the holder of the Salt Lake Western stock, is impracticable, then a substantial additional amount of new first-mortgage bonds should be allotted. It also suggests recognition of the lease value by capitalizing a part of the future rental. The committee takes the position that these claims of the Finance Corporation with respect to recognition of the Salt Lake Western rental values are untenable.

Our conclusion in this matter is that in the absence of a decision by the court on the above-mentioned petition, or of some other appropriate action determining the amount of the Salt Lake Western trustee's claim for the debtor's use and operation of its property, it would be inappropriate for us to attempt to assign any given value to the claim for rental. However, we cannot ignore the possibility that this claim may be determined by the court to have a value. For that reason, we are of the view that we should dispose of the matter now by providing in the plan for such eventuality.

This we do by the provision that, in the event the rental or other use-and-occupation claim of the Salt Lake Western trustee against the debtor's trustees is allowed in whole or in part by the court, the money value of the award shall be deducted from the total claim, with corresponding adjustment on a ratable basis, of the allocations, both directly and to pledged securities of new securities herein allotted to the total claim. The adjustments thus made in the allotments of securities should not change the allotments of securities to creditors other than the Finance Corporation but should be effected by making appropriate change in the new securities issuable to the Finance Corporation under the plan. The foregoing provision for the claim for rental should be applied regardless of whether or not consolidation is effected under the plan.

The examiner's recommendation, in case there is to be no consolidation, was that new securities be allotted to the pledged securities of classes that are publicly held, on the basis of the new plan, and that, for the remainder of the claim, a 12-year collateral note for $7,500,000 be given the Finance Corporation, secured by the Salt Lake stock, Salt Lake Western stock, and the "outside" securities now under pledge. The Finance Corporation contends that, if consolidation with the Salt Lake fails, it is entitled to outright ownership of the collateral which it holds and that if it is deprived of such ownership an adequate recognition of its rights requires that the proposed 12-year secured note should be for a substantially larger amount than $7,500,000, should bear 4 percent fixed interest, and should be an actual obligation of the new company, rather than that the obligations of the new company should be limited to the proceeds of sale of the pledged securities and to the income from such securities, as suggested by the examiner.

We agree in principle with the Finance Corporation that it is entitled to the pledged securities in the event there is no consolidation. On a cash basis, however, it is not entitled to any amount in excess of its claim, and any equity in the pledged securities clearly would belong to the debtor's estate. We think, therefore, that to turn all the collateral over to the Finance Corporation outright would be unjustifiable. All the rights of the Finance Corporation will be recognized if all of the pledged collateral, including securities received for pledged securities of the principal debtor, be placed in escrow for the benefit of the Finance Corporation, and if it be permitted to negotiate a sale or sales of the collateral and to receive any funds yielded by the collateral through interest payments, dividends, or sales, until the claim shall have been liquidated, whereupon its right and interest in the remaining collateral would cease, and, on the other hand, if the claim shall not have been

fully satisfied within a specified period by such payments, the securities, or the portion thereof remaining undisposed of, would be reduced to possession by the Finance Corporation, subject only to the conditions that the new company be permitted at any time to acquire all of the securities remaining in escrow by payment of the balance due upon the claim of the Finance Corporation, and to purchase all of the stock of the Salt Lake and Salt Lake Western which the Finance Corporation shall have requested the escrow agent to sell, at the price or prices stated in the request. The purchase of such stock by anyone other than the new company should be subject to our approval.

Such an arrangement would, in effect, assign the pledged collateral to the Finance Corporation to the extent necessary for the full settlement of its claim, any securities remaining thereafter to revert to the new company. We think that a period of 6 years would allow all reasonable opportunity for a sale of the Salt Lake or Salt Lake Western stock, if such a sale be practicable, or any other suitable disposition of the deposited securities. During this period the Finance Corporation should be entitled to vote all the stocks held in escrow.

This provision for an alternate treatment of the Finance Corporation's claim, in the event there is no consolidation, is included in appendix B, showing the capital structure and distribution of securities approved on that basis.

Claims of the bondholders.—As has been stated, the distribution of new first-mortgage bonds and income bonds under the plan now approved is in accordance with the percentage distribution shown, based on the original earnings formula as adjusted. The allocation of new securities to the several classes of claims is set out in appendix A. The percents of claim shown represent adjustments to the nearest even figure from the percents developed by the formula, as set out in appendix C.

The Rio Grande Western first-trust mortgage is secured by a first lien on approximately 415 miles of line, of which 314 miles are main line between Crevasse and Ogden, Utah, and on equipment having a ledger value, less depreciation, of $17,637, as of December 31, 1936.

Preferred treatment of the bonds was given in the early plans developed under the earnings formula, because of the earnings available for interest, averaging about 1½ times requirements, and the high traffic density on this part of the system. The $15,190,000 of bonds outstanding in the hands of the public, bearing interest

at 4 percent per annum, matured on July 1, 1939. With interest accrued to January 1, 1942, the claim amounts to $19,443,200.

In the court plan, the claim (as of January 1, 1941) was to be settled on the basis of approximately 80 percent in new first-mortgage bonds and 20 percent in new income bonds. The committee accepts this treatment, as a concession to facilitate an early reorganization, but urges a modification of the terms of the new first-mortgage bonds to provide that the prior contingent interest thereon shall become fixed interest when the sum of fixed and prior contingent interest shall have been earned 1½ times in each of the 3 calendar years in any 5 successive calendar years, provided that such 3 years include the last 2 of such 5 years. The committee proposes that this provision apply to all new first-mortgage bonds issued in reorganization, as has been stated. We do not approve this provision. In our opinion, adequate treatment is afforded those receiving the new first-mortgage bonds through the provision that the contingent-interest payment of 1 percent is to be prior to other contingent interest and fully cumulative. The increase in fixed-interest requirements which would result from this provision is not justified by the record.

The Rio Grande Western first consolidated mortgage represents a second lien on the property subject to the first lien of the first trusts, and a first lien on approximately 283 miles of branch lines, the entire capital stock of the Utah Fuel Company, and equipment, having a ledger value, less depreciation, of $681,191, as of December 31, 1936. The $15,080,000 of bonds outstanding in the hands of the public, bearing interest at 4 percent per annum, will mature on April 1, 1949. With interest accrued to January 1, 1942, the claim amounts to $19,453,200.

Under the court plan, preferred stock was allocated to this claim. The parties contend that income bonds should be allotted for portions of the claim, ranging from 25 percent to 35 percent. Such contentions contemplate a much larger total amount of income bonds that we are now approving.

The distribution formula shows no earnings directly for the Rio Grande Western consolidateds, but they are entitled to any new bonds assignable to the first trusts in excess of the amount of that claim. On the basis of the total amount of new first-mortgage bonds and income bonds available under the capital structure herein approved, the spillover for the consolidateds consists of income bonds equaling approximately 6 percent of the total claim. Preferred stock is allocated to 69 percent of the claim, and common stock to the balance.

The debtor's formula gives effect to the lien on the stock of the

Utah Fuel Company, to the extent that the mortgage is credited with $83,333 for the annual earnings of the fuel company. This credit is of no practical effect, however, because of the large deficit in net railway operating income computed. The evidence as to the fuel-company property, which we have already mentioned, raises serious doubt that the foregoing figure represents the real earnings of the fuel company. In our opinion, these bondholders are entitled to receive the beneficial interest in the Utah Fuel Company stock, in addition to the reorganization securities allotted to them. The approved plan so provides.

The Junction first mortgage represents a first lien on the 62.08 miles of main line between Rifle and Grand Junction, Colo. There are $2,000,000 of bonds outstanding, matured on December 1, 1939, bearing interest at 5 percent. The total amount of the claim, with interest accrued to January 1, 1942, is $2,658,333.

In all the plans prepared, these bonds have received the same treatment as the Rio Grande Western first trusts, on the basis of full coverage of interest requirements and high traffic density. The earnings formula herein followed supports this treatment. Our allotment of new securities is the same as for the first trusts, i. e., on the basis of 71 percent in first-mortgage bonds and 29 percent in income bonds.

Among the debtor's objections to the court plan was the point that the Junction is not a debtor under section 77. All other parties have evidently assumed that the Junction could be merged or consolidated in the new system although it is not in trusteeship. It has no separate operating organization. The property was leased by the debtor on January 1, 1890, for a term of 50 years, and the leasehold interest is in trusteeship. The trustee has continued to operate the property since expiration of the lease, without renewal. Its stock is pledged under the Denver's refunding and improvement mortgage. The trustee of the Junction mortgage is also the trustee of the Rio Grande Western first-trust mortgage, and its counsel have always discussed the two claims on the same basis with respect to the plan and the rights of the two classes of bondholders. The court plan made no distinction because of the fact that the Junction is not in trusteeship. We shall not attempt to adjudicate the question but shall provide for the inclusion of the Junction in the plan, with provision for its consolidation into the reorganized company.

The D. & R. G. first consolidated mortgage represents a first lien on approximately 875 miles of standard-gage and 683 miles of narrow-gage line, including the debtor's main line from Denver to Rifle via Pueblo, and an 18-mile section between Grand Junction

and Crevasse. Also covered by the lien is equipment having a ledger value, less depreciation, of $4,708,523, according to the debtor's statement of the various mortgage liens, introduced at the 1937 hearings.

The bonds issued under this mortgage and outstanding in the hands of the public comprise $34,125,000 of 4-percent bonds and $6,382,000 of 4½-percent bonds, all of which matured on January 1, 1936. The total amounts of these claims, as of January 1, 1942, were $44,362,500 and $8,535,925, respectively. The distribution formula indicates that new first-mortgage bonds should be allotted to approximately 23 percent of the total claims, and new income bonds to approximately 10 percent. The remainder of the claim is allotted preferred stock and common stock, as shown in appendix A. In the court plan, the allotment of new first-mortgage bonds was for approximately 28 percent of the claim, and of income bonds approximately 16 percent.

The debtor's refunding and improvement mortgage represents a first lien on approximately 85 miles of standard-gage and 34 miles of narrow-gage branch lines, a junior lien on all other lines owned, and a first lien on equipment having a ledger value, less depreciation, of $7,268,622, according to the debtor's evidence at the 1937 hearings. A question arose as to part of the equipment, having a depreciated value of $1,333,252, and, as stated in our report, 233 I. C. C. 515, at page 570, a compromise agreement was reached by the interested parties whereby the equipment in question was deemed to be subject to the lien of the D. & R. G. consolidated mortgage. There are pledged under the refunding and improvement mortgage the shares of Junction stock, less directors' qualifying shares, the stocks of the three terminal companies hereinbefore mentioned, and $906,000 of the Junction's refunding bonds.

The issues of bonds under this mortgage include $2,000,000 of series A 6-percent bonds, due on October 1, 1974, and owned in equal parts by the Missouri Pacific and the Western Pacific Railroad Corporation, and $22,481,000 of series B 5-percent bonds, due on April 1, 1978. Of the series B bonds, $4,385,000 are pledged with the Finance Corporation and $6,096,000 are pledged with the Chase National Bank, leaving $12,000,000 outstanding in the hands of the public. The total amounts of the claims, as of January 1, 1942, were series A, $2,870,000, and series B, $16,350,000, a total of $19,220,000.

Under the distribution formula and the plan herein approved, each of these claims is recognized by the allotment of new first-mortgage bonds for 18 percent, new income bonds for 8 percent, and preferred and common stocks for the balance, as shown in

appendix A. In the court plan, the corresponding percents for the new bonds were 28 and 16.

For the properties under the first lien of the refunding and improvement mortgage, as of December 31, 1935, the report of the Bureau of Valuation showed $12,121,243, as the cost of reproduction new, less depreciation, plus lands and rights, which is far below the amount of the claims. As we stated in our report, 233 I. C. C. 515, at pages 570–571, the depreciated book value of the equipment subject to the direct first lien of this mortgage, as of December 31, 1936, was $6,005,357, and that of the equipment subject to the first lien of $1,805,000 of equipment-trust obligations was $6,575,955. If subsequent depreciation and retirements are considered, not to mention large acquisitions of more efficient equipment, the foregoing amounts would seem to represent maximum values for the equipment. In our adjustment of the debtor's earnings formula, the refunding and improvement mortgage received the benefit of an increase from 2 percent to 4 percent in the rate charged for use of equipment.

Our adjustment of the formula also eliminated the alleged loss in operating the branch lines subject to the lien of this mortgage. This further increased the earnings computed for the refunding and improvement bonds, but no attempt was made to allow for the system revenue which was contributed by the branch traffic, approximating $1,500,000 a year.

As we have indicated earlier, the formula reflects a distribution of the charges paid by the Denver in connection with the three terminal companies, so it would be improper to take these properties into account in alloting new securities to the claim of the refunding and improvement bonds.

The debtor's general mortgage represents a lien generally upon the property securing the refunding and improvement mortgage but junior thereto. Under the general mortgage, there were issued $29,808,000 of bonds, bearing 5 percent interest, and maturing in 1955. The total claim, as of January 1, 1942, is stated by the mortgage trustee at $42,057,755. The court plan assigned new no-par common stock to this claim on the basis of approximately 3⅓ shares for each $1,000 of claim. The mortgage trustee urges an allowance of 50 percent in new common stock, arguing that the improvements made on the railroad and its recent earnings justify a larger capitalization than that contemplated by the court.

We have given careful consideration to the court plan and the later evidence as to earnings, but, within the framework of the capital structure which we have now decided upon, the maximum allowance for this claim is that shown on appendix A, viz, one-half

share of common stock, having a par value of $100 a share, for each $1,000 of claim.

From the foregoing considerations, we find that the provisions herein made for the settlement of the claims described above will afford full recognition of the rights of the holders of such claims and will be fair and equitable to all parties.

The holders of bonds of the classes shown below should receive for each $1,000 bond and all unpaid interest thereon, as of the effective date of the plan, substantially the following amounts of new securities: Rio Grande Western Railway Company first-trust bonds, $908.80 of new first-mortgage bonds and $371.20 of new income bonds; Rio Grande Western Railway Company consolidated-mortgage bonds, $77.40 of new income bonds, $890.10, par value, of new preferred stock, and $322.50 of new common stock; Junction first-mortgage bonds, $943.71 of new first-mortgage bonds and $385.46 of new income bonds; Denver & Rio Grande Railroad Company consolidated-mortgage 4-percent bonds, $299.00 of new first-mortgage bonds, $143.00 of new income bonds, $286.00, par value, of new preferred stock, and $572.00, par value, of new common stock; Denver & Rio Grande Railroad Company consolidated-mortgage 4½-percent bonds, $307.63 of new first-mortgage bonds, $147.12 of new income bonds, $294.25, par value, of new preferred stock, and $588.50, par value, of new common stock; the debtor's refunding and improvement 5-percent bonds, $245.25 of new first-mortgage bonds, $109.00 of new income bonds, $286.13, par value, of new preferred stock, and $722.12, par value, of new common stock; the debtor's refunding and improvement 6-percent bonds, $258.30 of new first-mortgage bonds, $114.80 of new income bonds, $301.35, par value, of new preferred stock, and $760.55, par value, of new common stock; the debtor's general-mortgage bonds, $70.55, par value, of new common stock.

The provision for scrip will be as in our former plan.

Salt Lake bonds and stock.—Under the terms of the Salt Lake income mortgage, interest becomes fixed at 6 percent if consolidation with another road is effected. During the 10-year period 1931–40, the earnings of the Salt Lake available for interest averaged 4.34 percent per annum on the amount of income bonds outstanding and the average payment was 4.2 percent. From 1928 to 1931, and in 1935, 6 percent was paid. The available income during the 10-year period averaged $478,000. This sum approximates the annual income indicated by the severance study, hereinbefore mentioned, as representing the contributive value of the cut-off to the system. The court plan provides that the holders of the income bonds be

offered 4 percent fixed interest, and it is desirable that every reasonable inducement be made in order to effect the consolidation. But, as the committee's analysis of the situation with respect to relative earnings, et cetera, shows, the allowance of 4 percent fixed interest on the Salt Lake incomes is evidently unjustified when the new first-mortgage bonds offered to the debtor's bondholders and the Finance Corporation are to bear 3 percent fixed interest and 1 percent prior contingent interest, and moreover are not to be issued for the full amount of these claims. A further consideration is the fact that the percent of new first-mortgage bonds allocated to the Western present mortgages in the court plan is materially reduced in the plan herein approved.

As above stated, the court plan made the consolidation with the Salt Lake subject to the consent of the holders of at least 66⅔ percent of the income bonds outstanding. Including the bonds pledged with the Finance Corporation, the total principal amount outstanding is $11,000,000, and, if only 66⅔ percent assent to the plan, the nonassenting bonds would amount to $3,666,666.67. The refinancing of such an amount would, in our opinion, place an unduly heavy burden on the new company. We conclude that the required percent of assents should be 90, in order to avoid this difficulty. This figure is not an unusually high one in similar cases where a creditor group is asked to join voluntarily in a general plan of financial readjustment.

We find that the proposal to be submitted to the holders of the Salt Lake income bonds should provide for (1) an extension of the maturity of the bonds to the maturity date of the first-mortgage series A bonds to be issued by the new company, (2) the modification of interest terms to fixed interest of 3 percent per annum, and prior contingent cumulative interest of 1 percent per annum, payable when fixed and contingent interest, respectively, on the new first-mortgage bonds become payable, subject to the right to postpone any interest payments with the consent of the holders of three-fourths of the bonds outstanding, as in the case of the new first-mortgage bonds of the new company, and (3) the call for payment, or for refunding (at the convenience of the reorganized company), of income bonds not consenting. If the holders of not less than 90 percent of the total income bonds outstanding consent to the foregoing conditions within 90 days from the submission of the proposal to them, the properties of the Salt Lake will be merged or consolidated with those of the new system, including the Salt Lake Western, the Junction, and the Goshen Valley. The new company will then assume the fixed-interest obligation of the Salt Lake first-mortgage bonds. No additional issues of bonds

under the Salt Lake mortgages will be permitted. The liens of these mortgages will remain undisturbed, and the lien of the new company's mortgages will be junior thereto with respects to the Salt Lake properties.

The amount of Salt Lake stock outstanding in the hands of the public has been increased from 460 shares, shown in our previous reports, to 4,111 shares as a result of the release of 3,651 shares by the Finance Corporation. New income bonds were allotted to these minority holdings of stock in our former plan, the court plan, the proposed report plan, and the modification of the latter suggested by the committee. Such treatment is admittedly liberal in view of the treatment which we have given herein to the majority Salt Lake stock pledged with the Finance Corporation, and also in view of the reduced capital structure now contemplated. Moreover, an allotment of income bonds would tend to dilute the total issue. We accordingly find that substantial justice will be done by providing that the Salt Lake minority stockholders receive new preferred stock on the basis of 1 share for each share of Salt Lake stock. Since the Salt Lake is not in trusteeship, the action taken by the stockholders with respect to this offer will necessarily be voluntary, and if the holders of the Salt Lake income bonds reject the proposal to modify the terms of such bonds the offer to the stockholders will not be made and the stock will remain undisturbed.

Other claims.—The claim of the Chase National Bank on its note of $1,500,000 with interest at 6 percent from the date of the filing of the debtor's petition under section 77, in accordance with the contentions of the bank, amounts to $2,068,458. The proper interest rate to use in computing this claim has not been determined by the courts. Subject to such determination, as stated in our former plan, the note should be extended for a term of 10 years, bearing interest at 4 percent per annum, payable semiannually, but such interest should be contingent upon, and the payment thereof should be limited to, the total of interest and dividends paid by the new company on the collateral securing the new note or notes. The provisions of our former plan for the claim of the Chase National Bank should be modified only with respect to the new collateral to be pledged. The present collateral consists of $6,096,000 of the debtor's refunding and improvement mortgage 5-percent bonds. With accrued interest to January 1, 1942, the amount is $8,305,800. Under the plan herein approved, the new securities allocable to it consist of $1,495,044 of first-mortgage bonds, $664,464 of income bonds, $1,744,218 of preferred stock, and $4,402,074 of common stock. The plan provides for the pledge of these securities as collateral security for the new note.

The Railroad Credit Corporation, in its brief, explains that, as of June 30, 1941, the unpaid balance of the original loan of $500,000 had been reduced to $266,715.09 owing to the application of distributive shares credited against the debtor's account arising out of the fund administered by the Credit Corporation, and the amount of unpaid interest was $904.88, making a total claim of $267,619.97. Explanation is also made of an error in the statement by the court of the amount of the claim as of January 1, 1941.[6] The Credit Corporation advises that the amount of its claims, as of January 1, 1942, was $265,194. In its exceptions to the examiner's proposed report, the Credit Corporation states its position with respect to the court plan as follows: It objects to the court's proposal for the reason that the court proceeds on the theory that the Credit Corporation is indebted to the debtor, and, in providing for payment of its claim in cash, the judge deducted from the claim the debtor's undistributed book balance, which includes income earned upon the marshaling and distributing fund. Under the theory outlined in the court plan, distribution of more than 100 percent of the debtor's contribution to the fund would have to be made. The Credit Corporation states that is hardly to be expected. It contends that distributive shares do not constitute a debt to the debtor unless and until funds are available and a distribution is actually declared, set aside, or made.

The provisions for the Credit Corporation claim as stated in our modified plan will be retained, with appropriate revision of the amounts of new securities issuable against the $662,000 of D. & R. G. consolidated-mortgage 4-percent bonds, which, with interest accrued to January 1, 1942, amount to $860,600. The new securities allocable under the plan herein approved consist of $197,938 of first-mortgage bonds, $94,666 of income bonds, $189,332 of preferred stock, and $378,664 of common stock.

All equipment obligations of the debtor outstanding, any equipment-trust certificates which may be issued by the bankruptcy trustees or any other obligations under equipment leases or sales agreements, will be assumed or paid by the new company when they respectively become due. The interest of the holders of such obligations shall be deemed not to be adversely and materially affected by the plan, and submission to the holders shall not be necessary. The plan should not be construed as prohibiting the assumption of obligation and liability in respect of additional equipment obligations prior or subsequent to its consummation, if duly authorized under section 20a of the Interstate Commerce Act.

[6] The court plan provided for the payment of the balance of the claim in cash after deducting the amount due the debtor under the marshaling and distributing plan.

Future control.—The trustee of the Missouri Pacific contends that an equity exists for the debtor's present stock, that the Missouri Pacific should be permitted to acquire 50 percent of the new common stock on fair and reasonable terms, and that voting control should be lodged solely in the common stock, as it is at present. Counsel for the debtor contend that provision should be made for allotting management stock to the debtor with conditions attached defining the extent of any contribution that should be required from the debtor whether for management stock alone or for management stock and "securities secured on debtor's wants."

We have reaffirmed our previous finding that the equity of the debtor's stockholders is of no value. In our prior report, 233 I. C. C. 515, at page 581, we said:

> As we view the matter these are not questions for us to decide in promulgating a reorganization plan where we find that the present stockholders have no equity, and we do not consider it our duty in this case to decide for the new owners what affiliations with other systems will be most advantageous to the new company, or to fix a price for any stock which may be offered to the Missouri Pacific, Western Pacific, or other railroad companies. In order, however, to facilitate any reasonable plan which the new stockholders may adopt with respect to the acquisition of an interest by a larger system or systems, the following provision for the stock should be incorporated in the reorganization plan.

We have given consideration to all the representations which have been made in this connection, including the court's proposal to make the income bonds assigned to the Finance Corporation convertible into management stock, and have concluded that we should adhere to our position as previously stated, which, in effect, leaves the matter of control of the new company to future determination.

In the proceedings before the court, the Public Service Commission of the State of Utah renewed its previous objections to the merger or consolidation of the Salt Lake, as contemplated under the plan certified to the court. The same objection may be made to the plan herein approved. It is predicated on the belief that if the Salt Lake were kept separate the building of an extension from Craig, Colo., westward to Provo or Salt Lake City would be facilitated. This impelled the Utah interests to oppose the Denver's acquisition of control of the Salt Lake. As stated in our report, 233 I. C. C. 515, at page 550, our opinion is that a consolidation of the roads will not alter the present situation in such a way as to prejudice the construction of an extension westward through the Uintah Basin of Utah.

New-money requirements.—The amount of new money required in the reorganization will depend on the extent to which the trus-

tees may be able to pay off their outstanding certificates prior to consummation of the plan, the amount of cash available for the expenses of reorganization not already paid, and the provision to be made for the nonassenting income bonds of the Salt Lake.

Counsel for the committee, in their exceptions to the proposed report, assert that all the trustees' certificates may be paid before effectuation of the plan, and that, as a minimum, not less than $2,000,000 of certificates will have been paid without the need for new money. In support of this contention, counsel presented estimated income accounts, prepared by the respective managements of the Denver and the Salt Lake, for the year 1941, with the last 4 months estimated, indicating that the combined earnings available for interest would be $5,116,049, as compared with an estimate of $3,513,590 made at the hearing in May 1941. Also presented was a copy of a letter from the debtor's trustees stating their intention to begin paying off the certificates on February 1, 1942, and to continue to pay them off as soon as the resources will permit, subject to declines in traffic, increases in pay rolls, the approval of the court, et cetera.

By its report of August 26 1940, in this proceeding, 242 I. C. C. 629, division 4 fixed maximum limits of allowance for compensation and expenses of trust companies, committees, their counsel, et cetera, up to May 20, 1940, in the total amount of approximately $268,000. Previously, approximately $225,000 had been paid out of the debtor's estate, largely as compensation of the trustees, their counsel, and technical advisers. It is clear that our former estimate of $1,000,000 for total reorganization expenses does not apply to the present situation and that plan should be revised accordingly.

It is evidently impossible to estimate closely the amount of money which will be required to pay or refund the Salt Lake income bonds, the holders of which reject the proposal for modification of interest, et cetera, if the assents required for consolidation are obtained. The plan provides that the payment or refunding of the nonassenting bonds will be at the convenience of the new company. There will be no obligation upon the new company to redeem these bonds, although the incentive to do so would arise from the fact that 6 percent interest would be payable if the lines should be consolidated.

The actual earnings of the Denver available for interest in 1941 were reported at $4,503,690, and those of the Salt Lake at $515,746, a total of $5,019,436.

The Denver's actual cash position at the close of 1941 is shown by balance-sheet figures as follows: Cash on hand, $4,460,157; total current assets, $11,828,589; and total current liabilities, $10,-

292,313. For present purposes, there are deductible from total current liabilities the Chase Bank loan of $1,500,000, the Railroad Credit Corporation loan of $264,966, and $1,950,000 of the Finance Corporation loan. The result is net current assets of $5,251,242. The corresponding figure for the Salt Lake is $153,384.

The district judge stated in his recent opinion that the trustees considered that they should have a working balance of not less than $1,250,000. At the further hearing before us, the debtor's general auditor testified that $2,000,000 would be ample.

The Denver's cash position should permit the early application of about $3,750,000 to the payment of trustees' certificates, leaving $1,250,000 outstanding. To the latter amount may be tentatively added $1,000,000 to be used for the payment or refunding of non-assenting Salt Lake income bonds, in the event of consolidation, or for the payment of reorganization expenses, as circumstances may require. The plan accordingly provides (1) for a new loan in the amount of $2,250,000, subject to such increase or decrease as may be determined by the reorganization committee and approved by the court, but in no event to exceed $4,000,000, such loan to be obtained either from the Finance Corporation or through private channels, and secured by new first-mortgage bonds issued for that purpose in an amount equal to 125 percent of the amount of the loan, or by such other amount as shall be required by the lender and approved by us; and (2) as an alternative to such a loan, the plan provides that not exceeding $5,000,000 of new first-mortgage bonds may be issuable for sale to provide the new money required, as may be determined by the reorganization committee and approved by the court.

Voting trust for new stock.—The modified plan previously approved provided that all the preferred stock and common stock of the new company, except shares issued to qualify directors, should be deposited under an escrow agreement for a term of 10 years and that the voting trustees, subject to our approval, and with the consent of the holders of escrow receipts representing not less than a majority of the shares of preferred stock and common stock, respectively, might sell all or any part of such stock at such price or prices as might be deemed advantageous to the interest of the new company and its stockholders.

The court plan provided that the consent of two-thirds of the holders of class A common stock would be required for a sale. We approve this provision if restated so as to apply to the holders of escrow receipts representing not less than two-thirds of the stock. Giving effect to this change, the approved provisions for the voting trust will be as follows:

All the preferred stock and all the common stock issued by the new company in reorganization, excepting shares issued to qualify directors, shall be deposited under an escrow agreement with a bank or trust company designed by the court, and escrow receipts issued to persons entitled to receive such stock under the plan. The escrow agreement shall be for a term of 10 years from the date of creation of the trust, such term to be considered as beginning not later than 6 months after the confirmation of the plan, and shall provide that the reorganization committee, as voting trustees, may, subject to the approval of the Commission, and with the consent of the holders of escrow receipts representing not less than two-thirds of the shares of preferred stock on deposit, sell all or any part of such preferred stock at such price or prices as they may deem advantageous to the interest of the new company and its stockholders; likewise the voting trustees may sell all or any part of the deposited common stock, with the consent of the holders of escrow receipts representing not less than two-thirds of the shares of such common stock.

It shall be provided that all holders of escrow receipts shall be bound by the terms of any sale or sales which shall have been approved by this Commission and consented to as aforesaid, and the net proceeds of any sale or sales, together with any unsold stock, shall be distributed pro rata among the holders of the escrow receipts for preferred stock and common stock, respectively, according to the class of stock sold. During the life of the escrow agreement, the holders of escrow receipts shall have the right to receive notice of all meetings of stockholders and to direct the voting trustees as to the manner in which the stock represented by the escrow receipts shall be voted at such meetings. In the absence of such directions, the deposited stock shall be voted in such manner as the voting trustees may determine. The reasonable compensation and expenses of the voting trustees, including counsel fees, shall be paid by the new company.

Reorganization committee.—Our former plan provided for a reorganization committee consisting of five members, two to be designated by the committee, one by the trustee under the debtor's refunding and improvement mortgage, one by the trustee under the general mortgage, and one by the Finance Corporation. The judge, pointing out that the properties of the debtor and secondary debtor are located almost wholly in the States of Colorado and Utah, urges that all the members of the reorganization committee be residents of these States, that all meetings of the committee be held in Denver, at the main office of the debtor, and that counsel

for the committee, if any are necessary, shall be appointed by the court. Later, the judge expressed the opinion that the property should be under the direct control of the court until the reorganization is completed; also that the insurance-group committee should be represented by only one member on the reorganization committee and that the court or some other proper authority should name one member to represent the public interests of the citizens of Colorado. In line with the latter suggestion we approve the designation of one member by the court, and in lieu of one member each as representatives of the debtor's refunding and improvement mortgage and the general mortgage, we are of the opinion that these groups may properly be represented by one member, to be designated jointly by the two mortgage trustees. The total number of members will remain at five.

Provisions for new bonds.—The court proposed that the interest on the new 4½-percent income bonds shall be payable only to the extent of three-fourths of the income available for the payment thereof, and that it be cumulative only to the extent that payable interest is unpaid. It would seem, as pointed out in the brief of the committee, that the purpose of this provision may have been to permit the company to apply more of its income to additions and betterments than would be the case under the interest provisions of our plan for the new income bonds. The proposal now appears unnecessary and is not approved.

In connection with the new first-mortgage bonds to be issued in the reorganization, our modified plan provided that additional bonds shall be issuable under certain conditions, and included the following (239 I. C. C. 583, 600):

> [3*] When on any interest payment date the aggregate principal amount of first-mortgage bonds outstanding, plus all other funded debt bearing fixed interest, shall exceed either 35 percent of total capitalization as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding, the new company shall pay to the mortgage trustee as a sinking fund a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, the payment to the capital fund, contingent interest, and sinking-fund payments for the retirement of income bonds as hereinafter prescribed.

Counsel for the insurance group suggest that the foregoing percentage figures of 35 percent and 60 percent be increased to 45 percent and 70 percent, respectively, so that "this sinking fund will constitute only a practical check on injudicious financing rather than a harsh and impracticable constraint on the new company."

The plan which included this provision did not provide that the

Salt Lake bonds be treated in the manner that is now contemplated, nor that interest charges would be divided into fixed, prior contingent, and contingent classes. Under the capital structure herein approved, the ratio of total fixed-interest debt[1] to total capitalization will, at the outset, exceed 35 percent. We approve the change to 45 percent, in the case of consolidation, and 40 percent if consolidation is not to be effected. The provision in question will be modified to read substantially as follows:

(2) If consolidation with the Salt Lake is effected in accordance with this plan, and when on any interest payment date for first-mortgage bonds the aggregate principal amount of new first-mortgage bonds outstanding, together with Salt Lake first-mortgage bonds and income bonds, plus all other funded debt bearing fixed interest, shall exceed either 45 percent of total capitalization, as hereinafter defined, or the result obtained by deducting the principal amount of funded debt bearing contingent interest from 60 percent of the total capitalization at the time outstanding, the new company shall pay to the trustee of the new first mortgage as a sinking fund, a sum equal to 50 percent of the available net income of the preceding calendar year after providing for all fixed charges, prior contingent interest charges, the payment to the capital fund, contingent interest, and sinking-fund payments, as hereinafter prescribed; but, in the event such consolidation with the Denver and Salt Lake Railway Company is not effected, the foregoing requirement of 45 percent for total fixed interest bearing debt shall be 40 percent.

Counsel for the committee further request that the following provision of our modified plan* for the new first-mortgage bonds be omitted:

(4) No additional bonds of series A other than those to be issued under the plan may be issued, and no bonds may be issued of any series having a maturity on or before the maturity of the bonds of series A, except bonds issued on the basis of the acquisition of new equipment or to provide cash for such acquisition.

Counsel also request the omission of the corresponding provision (page 602) for the new income bonds reading:

(3) No income bonds other than those issued in connection with the plan shall be issued having a maturity on or before the maturity of the initial issue, except bonds issued on the basis of the acquisition of new equipment or to provide cash for such acquisition.

Our modified plan* also contained the following provision for the first-mortgage bonds, and a similar provision for the income bonds:

Additional bonds shall be issuable under the mortgage without limit as to amount, or within such limit as may be specified in the mortgage, having such dates, maturities, coupon rates, redemption, and sinking-fund provisions as may be determined by the board of directors and approved by this Commission.

[1] Including as such all the new first-mortgage bonds bearing 3 percent interest and 1 percent prior contingent interest.

* Page numbers omitted.

In making this request, the committee contends that the limitation imposed in our plan as to the maturity of later issues of bonds would make it impossible for the new company to finance its needs, however, urgent, by means of bonds. We are persuaded that the plan should be modified by eliminating the restriction in question. *Chicago, R. I. & P. Ry. Co. Reorganization*, 247 I. C. C. 533, decided July 31, 1941. We approve the change in the present case, and our order will so provide.

The provisions for the new first-mortgage bonds will be modified by introducing a general sinking fund, the annual payments to equal one-half of 1 percent of the maximum principal amount of such bonds at any time authenticated and delivered, including bonds under pledge. The payments into this fund should be made from the available net income remaining after fixed interest and prior contingent interest, but before contingent interest on the income bonds.

The concluding paragraph in section E of our order of April 2, 1940, 239 I. C. C. 583, referred to future modifications or alterations of the new first mortgage, and read in part as follows*—

> provided that no such change or modification shall (*a*) alter or impair the obligation of the new company to pay the principal and interest of any bond at the time and place and at the rate and in the currency provided therein without the consent of the holder of such bonds * * *.

The following addition to the paragraph above referred to is approved and will be incorporated in the plan.

> Notwithstanding the limitation in clause (*a*) in this paragraph, the obligation of the new company to pay interest on bonds issued in the reorganization for presently outstanding securities (and any other bonds as to which it may be so provided in the mortgage or any supplemental indenture) may be modified by the concurrent action of the new company and of the holders of not less than three-fourths in aggregate principal amount of such bonds then outstanding, so as to postpone the time of payment of any particular installments of interest, or any described number of installments of interest, until any fixed or determinable date or until the happening of any specified contingency, not in any case later than the date when the principal of such bonds shall be or become payable; but no postponement shall be made of any installment of interest in excess of a cumulative total of 10 semiannual installments excluding installments paid or as to which due provision for payment has been made; and before any such postponement becomes effective the holders of such bonds shall become, and until all postponed installments of interest be paid or due provision for payment thereof be made shall remain, entitled to elect the smallest number of directors necessary to constitute a majority of the full board.

* Page number omitted.

In addition to the foregoing modifications of plan, certain minor revisions of our prior order are approved so that the plan will conform more nearly to plans recently approved by us, and these changes are incorporated in the present supplemental order.

We conclude that, upon the record previously made, the record in the court proceedings, and upon further hearing held by us, the report and order of April 2, 1940, approving a modified plan of reorganization for the Denver & Rio Grande Western Railroad Company, debtor, and the Denver & Salt Lake Western Railroad Company, secondary debtor, pursuant to section 77 of the Bankruptcy Act, as amended, should be further modified as herein specified, and that, as thus modified, the plan will meet the requirements of section 77 (b) and (e) of that act, will be compatible with the public interest, and should be approved.

An appropriate supplemental order will be entered.

MILLER, *Commissioner*, dissenting in part:

My separate expression in our prior report in this proceeding, 233 I. C. C. 515, 591, is equally applicable here. It is also my opinion that the common stock here should be no-par instead of $100 par value.

COMMISSIONER ROGERS did not participate in the disposition of this case.

* * * * * * *

(The appendices attached to this report are here omitted, being reproduced, slightly modified, as appendices to the Commission's last report which is hereinafter printed in full.)

INTERSTATE COMMERCE COMMISSION

Finance Docket No. 11002

DENVER & RIO GRANDE WESTERN RAILROAD COMPANY REORGANIZATION

Submitted May 18, 1943. Decided June 14, 1943

Upon petitions, the modified plan of reorganization of the Denver & Rio Grande Western Railroad Company, approved on July 13, 1942, pursuant to section 77 of Bankruptcy Act, as amended, further modified and approved.[1]

Appearances as in prior reports, and also *Malcolm Lindsey* and *L. H. Larwill.*

Third Supplemental Report of the Commission

BY THE COMMISSION:

Within the statutory period of 60 days from the date of our second supplemental report and order herein, July 13, 1942, 254 I. C. C. 5, approving a further modified plan of reorganization for The Denver and Rio Grande Western Railroad Company, debtor, and The Denver and Salt Lake Western Railroad Company, secondary debtor, pursuant to section 77 of the Bankruptcy Act, 11 U. S. C. 205, petitions requesting its modification were filed (1) jointly by counsel for the insurance-group committee, the United States Trust Company of New York, trustee of the Denver & Rio Grande consolidated mortgage, the Guaranty Trust Company of New York, trustee of the Rio Grande Western consolidated mortgage, the Chase National Bank of the City of New York, trustee of the debtor's refunding and improvement mortgage, and the Untermyer family group, this joint petition being accompanied by a request on behalf of the Central Hanover Bank & Trust Company, trustee of the Rio Grande Western first-trust mortgage and the Junction first mortgage, that the plan be modified as proposed; (2) by the Reconstruction Finance Corporation; (3) by the City Bank Farmers Trust Company, trustee of the debtor's general mortgage; (4) by the trustee of the Missouri Pacific Railroad

[1] Previous reports: 212 I. C. C. 105 and 709; 217 I. C. C. 107; 224 I. C. C. 574; 230 I. C. C. 515; 239 I. C. C. 583; 242 I. C. C. 629 and 721; and 254 I. C. C. 5.

Company; and (5) by the Chamber of Commerce of Alamosa, Florence, Leadville, Montrose, Salida, and Pueblo, Colo., jointly.

The abbreviated titles of railroad companies and others as used in our prior reports are followed herein.

Answers to the joint petition of the committee and others were filed by the Finance Corporation, the Moffat Tunnel Improvement District, and the City Bank Farmers Trust Company. A reply to the petition of the Finance Corporation was filed by the committee and others.

Pursuant to the provisions of subsection 77 (e) of the act, we have proceeded to a reconsideration of the proceedings under subsection 77 (d).[2]

By the terms of section 77 (d) of the act, we may, after rendering a report and order in which we have approved a plan of reorganization, upon petition for good cause shown, filed within 60 days of the date of our order, and upon further hearing if we shall deem necessary, in a supplemental report and order, modify any plan which we have approved, stating the reasons for such modification.

In the joint petition, the parties ask that, if further information as to the proposed modifications is desired, or if we have doubts as to the propriety of making any of them, an opportunity be given the petitioners to file briefs and present oral argument, and, if we deem it appropriate, to present further evidence. None of the other parties requested a further hearing.

We have denied the debtor's request for a further hearing, filed on May 1, 1943. We have also denied the petition of intervention filed by George A. Gaston, and thus his petition for a further hearing to consider the rights and status of the first-mortgage bonds of the Rio Grande Junction Railway Company.

The district court held a hearing on October 23–24, 1942, on a petition for the payment of interest on the debtor's bonds, and held another hearing on April 14–16, 1943, on petitions for the payment of rental by the debtor's trustees for use of the Salt Lake Western property, and for the payment in full of the claim of The Railroad Credit Corporation. At the close of the hearing, the judge announced that he would authorize the payment of rental for the Salt Lake Western, the amount to be fixed later, and also the affirmance of the lease of the Salt Lake Western and the trackage agreement with the Salt Lake. The judge entered an order on April 15, 1943, approving the payment of the Credit Corporation's claim in full,

[2] Subsection 77 (e) provides in part as follows: "If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection 77 (d) hereof."

and the release of $662,000 of Denver and Rio Grande consolidated-mortgage 4-percent bonds, held as collateral. These bonds, which had been subject to the second lien of the Finance Corporation under the terms of its loans to the debtor, have been, or will be, turned over to the Finance Corporation.

We have given consideration to these developments since the issue of our prior report and order, and have considered the testimony adduced at the court hearings where it appeared to concern the plan of reorganization, notably the analyses made of the debtor's operation of the cut-off and the Junction lines. Our comments as to such testimony appear later herein.

The proposals for modification of plan and our conclusions in connection with them are as follows:

Effective date of plan.—Our order provided that the effective date of the plan would be January 1, 1942, which date would determine the extent to which the claims of the creditors would be capitalized in new securities. The plan permitted the reorganization committee, subject to the approval of the court, to cause the issue of new securities to be dated as of a date other than January 1, 1942, but only if the creditors who receive such issue of new securities shall receive the same treatment in respect of accruals of interest as if such issue of new securities had been dated January 1, 1942.

In their joint petition the parties suggest that the foregoing provisions be eliminated and the following substituted:

> The reorganization committee shall determine and fix the effective date of the plan at any time on or between January 1, 1942, and the first day of the calendar month next preceding the date when the new securities are ready for delivery, provided, however, that the effective date shall not be later than January 1, 1944, unless the Commission hereafter on application of the reorganization committee enters an order approving some later date; the Commission reserves jurisdiction to approve any later date on application of the reorganization committee and such approval shall not constitute a modification of the plan.
>
> The new securities shall be dated and shall bear interest, or dividends, from the effective date of the plan.
>
> The amounts of claims referred to in the plan, and the amounts of new securities to be allotted to such claims under the plan, are to be computed as of the effective date. The amounts of new securities to be allotted are to be determined by applying in the amounts of the respective claims remaining as of the effective date, after any cash payments, the percentages set forth in the plan and in the appendix (the dollar amounts of such claims and the dollar amounts of new securities allotted as set forth in the plan and in the appendix are for illustration only.)

The petition states that it is conceivable that eventualties (particularly in regard to taxes) which cannot now be clearly foreseen

might constrain some postponement to a date nearer the time of the actual delivery of the new securities, and that the reorganization managers should be given discretionary powers to deal with that business problem. Reference is made to the provisions regarding the effective date of plan in *Florida East Coast Ry Co. Reorganization*, 252 I. C. C. 731, decided August 10, 1942.

In the *Florida East Coast case*, a flexible date for the new general-mortgage bonds was possible, because payments of interest not specifically provided for in the plan would not affect the distribution of securities under the plan. No such special circumstances exist in the present case, nor have any of the other parties suggested a change in the effective date. In addition, to many changes in the provisions for the determination and application of available net income, the joint proposal might, if adopted, involve either a major increase in the capitalization fixed or a scaling down of the allotment to the most junior creditor class in order to maintain the capitalization. The proposal is not approved. However, as more than a year has elapsed since the effective date fixed in the plan of July 13, 1942, and a later date would more nearly conform to the time of issue of the new securities, we conclude that the date should be changed to January 1, 1943, and that the plan should be based on the amount of the claims outstsanding as of that date.

In connection with the matter of the effective date of plan, the Finance Corporation asks that, in view of its claim for compensation in respect of the rental of the Salt Lake Western and because of the dividends being paid on the Motorway stocks, the plan should provide that nothing therein shall be construed as limiting or in any manner affecting the right of the Finance Corporation to apply, in its discretion, the income on and the proceeds of the collateral held by it to or toward the payment of the principal or interest, or both, to or upon its claim against the debtor prior to the consummation of the reorganization. We approve this proposal. The provision will be added as the second paragraph of section J of our order.

Except as indicated, no change will be made in sections A and K of the order, quoted above, and no modifications are necessary in section G, describing the determination and application of available net income.

New money requirements.—Our report of July 13, 1942, stated that the Denver's cash position should permit the early application of about $3,750,000 to the payment of trustees' certificates, leaving $1,250,000 outstanding. To the latter amount, $1,000,000 was tentatively added for the payment or refunding of nonassenting Salt

Lake income bonds, in the event of consolidation, or for the payment of reorganization expenses, as circumstances may require. The plan provided for a new loan in the amount of $2,250,000, subject to such increase or decrease as may be determined by the reorganization committee and approved by the court, but in no event to exceed $4,000,000, such loan to be obtained either from the Finance Corporation or through private channels. As an alternative to such a loan, the plan provided that not exceeding $5,000,000 of new first-mortgage bonds would be issuable for sale to provide the new money required.

This provision was made upon the basis of the Denver's cash position at the close of 1941, and the trend of earnings then indicated. The amount of cash on hand was $4,460,157, total current assets were $11,828,589, and total current liabilities $10,292,313. After deduction of the Chase Bank loan, the Railroad Credit Corporation loan, and a portion of the Finance Corporation loan from the total liabilities, the resulting net current assets of the debtor were $5,251,242. The corresponding figure for the Salt Lake was $153,384. The debtor's trustees considered that they should have a working balance of not less than $1,250,000, and the debtor's general auditor testified that $2,000,000 would be ample. The $5,000,000 of trustees' certificates were paid in 1942. On this basis, the parties to the joint petition proposed that the provision for new financing through a loan of $2,250,000 be eliminated and that the amount of new first-mortgage bonds issuable to the creditors be correspondingly increased.

Evidence introduced at the court hearings in October 1942, and April 1943, showed that, during 1942, $2,282,106 of equipment obligations under conditional-sales agreements were paid, about $624,000 was paid on certain new equipment, and the debtor's cash on hand at the close of the year amounted to $10,050,150. The debtor's income account for 1942 shows $17,429,772 available for fixed charges, after railway tax accruals of $4,985,816. For the first 2 months of 1943, the income available for fixed charges was $2,443,963.

The present cash position and earning power of the Denver are adequate assurance that any probable amount of cash required for paying the remaining reorganization expenses and the refunding or payment of nonassenting Salt Lake bonds can be met from funds on hand. We conclude that the former provision for a loan of $2,250,000 should be eliminated as an item of the new capital structure, but that the plan should still permit the new company to negotiate a loan, if necessary, as suggested in the joint petition.

Accordingly, section L of the order will be modified to read as follows:

Any cash that may, in the judgment of the reorganization committee, be needed in reorganization, but in no event to exceed $2,000,000, shall be advanced by the Reconstruction Finance Corporation or obtained through private channels and evidenced by a collateral note of the new company for a term of 12 years, secured by pledge of new first-mortage bonds in an amount equal to 125 percent of the loan, or such other amount of bonds as may be required by the lender and approved by this Commission. As an alternative to such a loan, not exceeding $2,250,000 of new first mortgage bonds may be issued for sale to provide the new money required, under terms and conditions to be determined by the reorganization committee and approved by the court and this Commission.

New capital structure.—Under the plan of July 13, 1942, the total capitalization of the new consolidated company was to be approximately $154,521,612, including a total debt of $82,994,255. Total fixed-interest charges were approximately $1,766,966, prior contingent-interest charges $473,494, contingent-interest charges $1,009,185, and total charges ahead of dividends on the preferred stock $4,235,039 per annum. We found that the value of the properties for the purpose of this proceeding was $154,521,612 and that the total capitalization upon consummation of the plan should not exceed approximately that amount. We found that the total fixed-interest charges should not exceed approximately the amount above stated, and we approved a provision of the plan whereby the payment of fixed interest on the new first-mortgage bonds might be deferred with the assent of the holders of a stated proportion of the bonds.

Under this former plan, the equipment obligations as of January 1, 1942, were shown in total amount of $9,139,605, including $2,667,605 of obligations under conditional-sales agreements. As has been stated, the latter obligations have been paid in full. The remaining equipment obligations, under the trusts of series D, E, F, G, and I, amounted to $5,758,000, as of January 1, 1943. The introduction of this figure in the capital set-up instead of the former amount of equipment obligations results in a reduction of $3,381,605, which has been effected through cash payments, reflecting the increased earnings.

Under the plan as now further modified, the capitalization of the new consolidated company, based on the claims outstanding as of January 1, 1943, would be $155,173,127, consisting of the equipment obligations and Salt Lake bonds; the Chase National Bank note; $38,573,680 of new first-mortgage bonds; $29,750,184 of new income bonds; $32,531,220, par value, of new preferred stock; and $35,167,585, par value, of new common stock. The determination

of the amounts of the new first-mortgage bonds, new income bonds, et cetera, and the basis of the new allocations are described later. The plan, on the basis of consolidation, is shown in detail in appendices A and C, attached hereto. Total fixed-interest charges would approximate $1,694,941, prior contingent-interest charges $498,318, and contingent-interest charges $1,364,133; and, including the payments to sinking funds and the capital fund, the total charges before dividends on the preferred stock would be $4,584,689. The fixed-interest charges stated are less than in the former plan. We find that there will be adequate coverage of such charges.

The estimated gross outlay under the debtor's new-equipment program, which is the result of the war situation, is $8,772,000. The debtor expected to make a cash payment of $2,793,960 in 1942 on account of 1,000 gondola cars, of which 780 cars had been delivered, but the payment was deferred. Beside the gondola cars mentioned, the acquisitions include 6 Diesel freight locomotives, 300 dump cars, and 200 freight cars, all to be delivered during 1943. It appears that the entire $8,772,000 would be payable in 1943, and the 5-year amortization plan, which was begun in 1942, would be carried out. Improvements to old equipment are estimated at $596,146 a year. The proposed amortization charges on both present and proposed equipment, plus the estimated depreciation charges on present equipment, the estimated expenditures for improvements to present equipment, and the estimated charges to depreciation of roadway and structures will aggregate approximately $4,751,111 in 1943, and about $5,305,111 in each of the 3 succeeding years. In addition, the projects for general additions and betterments, authorized but not completed in 1942, called for an expenditure of approximately $3,100,000. Ad valorem taxes for 1942 were estimated at $470,000, railroad unemployment taxes at $700,000, and Federal and State income taxes at $1,300,000. Later testimony indicates that the railroad unemployment taxes amounted to about $608,000 and the Federal income-tax liability to about $1,760,000.

On a cash basis, the program for purchases of new equipment, the payments in connection with present equipment, the estimated amount of taxes payable, and a reasonable allowance for general additions and betterments require a total outlay of approximately $16,600,000. Assuming the plan in effect as of January 1, 1943, the interest charges and payments to the capital fund and sinking funds would total $4,584,689. The sum of the two amounts is $21,184,689. If the combined income available for interest and taxes in 1942 is equaled in 1943, and if it be added to the total cash on hand as of December 31, 1942, the total will be approximately $36,-

858,000. On this basis, the total cash on hand at the close of 1943 will amount to about $15,600,000.

On an income-account basis, the cash payments for the new equipment would be charged to capital account and the charges to depreciation and amortization of equipment would be introduced as operating expenses. The proposed charge of $700,000 for depreciation of roadway and structures would also be made in 1943. Including the additional taxes, additions and betterments, interest payments under present equipment trusts, proposed improvements to present equipment, and the charges under the plan as stated above, the total deductions from available income in 1943 (if 1942 earnings were repeated) would be approximately $7,845,000, leaving a net available income of approximately $10,389,000 for 1943. As has been stated, the program required the payment of $8,772,000 in 1943 for the new locomotives and cars, and this would have to be paid out of cash resources.

It appears that on either the cash basis or the income-account basis the present earning power justifies the capital structure and annual charges under the plan herein approved, taking into consideration the new-equipment program, tax levies, et cetera, as they have been presented by the debtor's trustees. The traffic necessities of the war period probably account for as much as $10,000,000 of new investment, most of which is reflected in the amortization charges described.

We have reviewed in our previous reports the carriers' earnings record and have shown that in 1941, when the original improvement program was largely completed, the system income available for interest was $5,019,436. The committee's analysis of the earnings during the 5 years 1936–40, reflecting the unit costs of operation in 1940, indicated an average available income of $3,446,765 a year.

One of the debtor's trustees, at the court hearing in October 1942, referred to a report by the traffic department describing the new industries on the line and estimating that about two-thirds of them would continue in operation after the war. The gross revenues from traffic of $3,446,765, the total would be $6,446,765, and, if added to the earnings and $6,000,000 in 1944, with net revenues of possibly 50 percent of gross. If $3,000,000 be added to the above-mentioned average figure of $3,446,765, the total would be $6,446,765, and, if added to the earnings of 1941, the total would be $8,019,436. Under the new capital structure herein approved, the total charges before dividends on the common stock will be approximately $6,211,250, and the payment of a 5-percent dividend on the common stock would bring the total to $7,969,629. The

debtor's earnings in 1942 are recognized, but the uncertainties surrounding the economic situation negative any assurance of a long continuation of such earning power. Under the present program, the expenditures necessary to handle the abnormally heavy traffic incident to the war effort will be paid for out of the income produced by that traffic. It is not probable, in our opinion, that the debtor will have any large amount of excess revenue from this special traffic after these and other necessary charges are made. After consideration of the foregoing and all the information of record, we conclude that the value of the combined properties for the purposes of this proceeding is approximately $155,173,127 and that the capitalization of the reorganized system should not exceed approximately that amount.

As in the former plan, the effect of reorganization of the Denver without consolidation of the Salt Lake would be to eliminate from the new capital structure the $11,234,000 of Salt Lake bonds, the $411,000 of new preferred stock allocated to the Salt Lake stock outstanding in the hands of the public, and the new securities allocated directly to the claim of the Finance Corporation. The resulting new total capitalization of the Denver would be substantially $143,528,027, of which $76,240,322 would represent debt. Fixed-interest charges would total $1,742,945 per annum, including $556,-024 of interest on the Finance Corporation claim, which, however, as explained in the plan, is not to be an obligation of the new company but will be payable out of the proceeds of the securities to be placed in escrow for the benefit of the Finance Corporation. Total charges ahead of dividends would amount to $4,055,379. The plan on this basis is shown in appendixes B and C.

We find that there will be adequate coverage of fixed charges of the new company on the basis of reorganization without the Salt Lake, in the amount of $1,742,945, and that the value of the combined properties for the purposes of this proceeding, excluding the Salt Lake and Salt Lake Western, is approximately $143,528,-027.

New first-mortgage bonds.—The proposal to increase the allowable amount of new first-mortgage bonds by approximately the amount formerly fixed for new financing is approved. It will not increase the total capitalization or place any additional obligation on the new company.

The parties to the joint petition propose that the additional first-mortgage bonds be distributed 70 percent to the Rio Grande Western first trusts and the Junction bonds, the remainder going to the Denver & Rio Grande consolidated, the refunding and improve-

ment bonds, and the Finance Corporation, increasing the allotment to the Finance Corporation by approximately 1 percent of the former allotment. The reason given for the 70-percent treatment is that it would fill out the principal amount of the Rio Grande Western claim, as was done under the court plan, described in our prior report.

We are not persuaded that this method of distribution is fair to the creditors as a whole, and we are of the opinion that the modified amounts of first-mortgage bonds and other new securities should be allocated in the same manner as was followed in the plan of July 13, 1942. This will be more fully explained later. The modification of allocations sought by the Finance Corporation will also be discussed.

Section D of our order provided for a so-called excess-bond sinking fund, which, if consolidation is effected, would become operative when the amount of all funded debt bearing fixed interest exceeds either 45 percent of total capitalization or the result obtained by deducting the principal amount of funded debt bearing contingent interest, other than bonds issued under the first mortgage, from 60 percent of total capitalization.

In the joint petition, it is asked that the above figure of 60 percent be changed to 65 percent, and a similar change made in section G (6) of the order, so as to provide more initial leeway for additional first-mortgage bonds. The change is consistent with the plan suggested in the joint petition and also with the modified plan herein approved. It will be adopted accordingly.

In connection with the operation of the excess-bond sinking fund when consolidation is not effected, the joint petition requests no change in the provisions of our former order but points out that the plan should indicate that the $535,088 of annual interest shown on former appendix A as applicable to the Finance Corporation claim of $18,377,209 as of January 1, 1942, is not an obligation of the new company but is collectible only out of the securities to be deposited in escrow for the benefit of the Finance Corporation. Unless this be done, it is stated, the Finance Corporation claim might be deemed a fixed-interest debt and the excess-bond sinking fund on the first-mortgage bonds would immediately become operative. This is true both with respect to our plan of July 13, 1942, and the modified plan herein approved, and, although the provisions made under section K of our order as to the payment of interest on the claim are clear, we deem it advisable to add the suggested footnote on new appendix C referring to the interest item of $556,024, and reading as follows:

Payable only out of the proceeds of the escrowed securities and an obligation of the new company, as explained in the plan.

New income bonds.—Under the plan of July 13, 1942, on the basis of consolidation, the amount of new income bonds was $21,916,932, these bonds being allocated among the several claims as shown in former appendix A.

The proposal made in the joint petition is to fix the amount of income bonds at $29,816,062, an increase of $7,897,430. This would permit filling out the claims of the R. G. Western first trusts, the Junction bonds, and the Finance Corporation, and leave sufficient bonds with which to make increases in the allotments to the other groups. As justification for the proposal, the petitioners refer to the court plan, wherein $30,289,451 of new income bonds were shown, to the prospect of increased traffic from the plants recently located on the line, and to the desirability of giving the present creditors the benefit, in respect of railroad income taxes, of receiving bonds rather than stock for a portion of their claims.

Using round numbers, an increase of $8,000,000 in the total amount of new income bonds would increase contingent-interest charges by $360,000 a year, with a decrease of $400,000 a year in dividends, at 5 percent, on a like amount of preferred stock. It would increase the ratio of total debt to total capitalization from 53.7 percent to 58.9 percent. In the light of the debtor's earnings record, we find this change to be permissible. The modified plan herein approved shows an increase of $7,833,552 in the amount of income bonds, and the basis upon which the increased amount of bonds has been allocated is explained hereinafter. The allocations suggested in the joint petition are not approved.

New stock.—Since the amount and allocations of the new stock, both preferred and common, shown in the suggested plan accompanying the joint petition, are predicated on a distribution of senior securities which we do not approve, and as they are also based on the claims outstanding on January 1, 1942, it is unnecessary to discuss this treatment of the new stock. The attached appendixes show the amounts and allocations approved.

In connection with the allotments of new common stock under the plan of July 13, 1942, the trustee of the debtor's general mortgage objected to the assignment of $2,102,888 of stock to the claim represented by the general-mortgage bonds, this assignment being on the basis of 5 percent of the principal amount of the claim plus interest to January 1, 1942. The mortgage trustee, in its petition for modification of plan, directed attention to the improved earnings and operating efficiency of the road, urged the elimination of

the item of $2,250,000 for new money, and proposed that the common stock allocated to the general-mortgage bonds be increased by that amount. Later in its reply to the joint petition of the committee and others, the trustee contended that the total capitalization of the new company under the plan of July 13, 1942, was unduly conservative and should be modified by increasing the amount of common stock so that at least five shares could be allocated to each $1,000 of the claim of the general-mortgage bonds.

The first-mentioned request, if applied to a 5-percent allotment to the claim as of January 1, 1943, would mean adding $2,250,000 to $2,177,408, resulting in an allotment of $4,427,408, or 10.2 percent of the claim. Under the second request, it would be necessary to issue $17,346,669 more common stock in order to satisfy 50 percent of the claim, which would increase total capitalization by a like amount.

Substantial compliance with the trustee's first request is made possible as a result of eliminating the provision for immediate borrowing, which, by increasing the amount of new first-mortgage bonds, permits the issue of a corresponding additional amount of new common stock. The total capitalization is, therefore, not enlarged by assigning common stock to the general-mortgage bonds on the basis of 10 percent of the claim. The modified plan will so provide. The request for further increases in capitalization is inconsistent with our previous findings herein as to the value of the properties and is disapproved.

Allocation of new securities.—The new securities under the plan of July 13, 1942, were allocated to the various claims as of January 1, 1942, on the basis of the debtor's segregation formula, adjusted to reflect the system earnings during the period 1935–40, and further adjusted in respect of the claim of the Finance Corporation, as shown on former appendix C and fully explained in our report. The same formula has now been applied to the claims as of January 1, 1943, and to the amount of bonds and stock herein approved. The primary allocations have been modified by reducing the allotment of first-mortgage bonds to the Finance Corporation claim to $5,200,000. The facts and considerations upon which this determination is made are stated below under "Treatment of Finance Corporation claim." The detailed figures are shown in appendix D, which provides the basis for the other appendixes attached to this report, and supersedes former appendix C.

The holders of bonds of the classes shown below should receive for each $1,000 bond and all unpaid interest thereon as of the effective date of the plan, substantially the following amounts of

new securities: Rio Grande Western Railway Company first-trust bonds, $970.20 of new first-mortgage bonds and $349.80 of new income bonds; Rio Grande Western Railway Company consolidated-mortgage bonds, $266.00 of new income bonds, $970.90, par value, of new preferred stock, and $93.10, par value, of new common stock; Rio Grande Junction Railway Company first-mortgage bonds, $1,061.96 of new first-mortgage bonds and $317.21 of new income bonds; Denver & Rio Grande Railroad Company consolidated-mortgage 4-percent bonds, $318.92 of new first-mortgage bonds, $217.08 of new income bonds, $321.60, par value, of new preferred stock, and $482.40, par value, of new common stock; Denver & Rio Grande Railroad Company consolidated-mortgage 4½-percent bonds, $329.03 of new first-mortgage bonds, $223.97 of new income bonds, $331.80, par value, of new preferred stock, and $497.70, par value, of new common stock; the debtor's refunding and improvement mortgage 5-percent bonds, $250.01 of new first-mortgage bonds, $159.61 of new income bonds, $310.75, par value, of new preferred stock, and $692.13, par value, of new common stock; the debtor's refunding and improvement mortgage 6-percent bonds, $264.61 of new first-mortgage bonds, $168.94 of new income bonds, $328.90, par value, of new preferred stock, and $732.55, par value, of new common stock; and the debtor's general-mortgage bonds, $146.10, par value, of new common stock.

In view of the recent decision of the United States Supreme Court in *Institutional Investors Group* v. *Chicago, M., St. P. & P. R. Co.*, 318 U. S. ——, we deem it desirable to set forth our conclusions as to the adequacy of the compensation flowing under the plan to the various classes of bondholders for the rights surrendered by them. These considerations are important, since the plan permits participation by interests wholly or partly junior to each of five of the debtor's mortgages, the liens of which have been described in our previous reports.

The Rio Grande Western first-trust 4's are not callable and are secured by a first lien on 412 miles of road, and 24 units of equipment,[3] the secured debt amounting to $48,680 per mile of road, without the equipment. The new first-mortgage bonds to be issued in exchange for 73.5 percent of the claim of the holders of these bonds are redeemable at an initial premium of not exceeding 5 percent, or such lesser amount as the reorganization managers may determine, and will constitute a first lien, in case of consolidation, on 1,731 miles of railroad, and the debt secured will be $22,284 per mile of first lien. They will constitute a junior lien on the 220

[3] These and similar figures stated later are based on the Bureau of Valuation report dated March 1, 1937, filed in this proceeding.

miles of the Denver & Salt Lake. The new income-mortgage bonds will be junior to the lien of the new first-lien bonds, and the debt secured, including all prior debt, will be $42,797 per mile of line on which the new first mortgage is a first lien.

While the old Western first-trust 4's required the payment of interest, together with interest on other securities, out of earnings between the levels of $445,932 and approximately $2,863,922, the securities to be issued in exchange for them, i. e., new first-mortgage and income-mortgage bonds, will require payments of interest out of earnings between the levels of approximately $139,089 and $4,506,979. The latter is the limit of earnings necessary for the interest payment on all the income bonds after a capital-fund charge of $750,000 and a sinking-fund charge of $200,489 for the benefit of the new first-mortgage bonds, imposed in the plan. The old securities, which matured in 1939, bore interest at the rate of 4 percent per annum. The average rate of the new securities to be received in exchange under the plan, i. e., first-mortgage and income-mortgage bonds, is 4.13 percent. Unpaid interest on the income bonds is cumulative to 18 percent. They have the benefit of a sinking fund provided for at the rate of one-fourth of 1 percent of the maximum amount of the bonds issued, or $76,808 for the amount of bonds provided for in the plan.

Since the old first-trust 4's have matured, their interest rate is not determinative of the income which the holders of these bonds should receive either in kind or in some equivalent form of compensation from the securities received in exchange.

The surrender of income position of the first-trust 4's results wholly from the allocation of income bonds for 26.5 percent of the claim. When it is considered that the sinking-fund and the capital-fund payments are responsible for $950,489 of the apparent loss of approximately $1,700,000 of income position, it appears that such loss is of small moment: The sinking fund is provided, and would be used, to retire the debt ahead of the incomes, and the capital fund is for a purpose for which expenditures would have to be made to keep the property in a position to perform its function, even under the old capital structure. Finally, since 73.5 percent of the new securities allotted to the first-trust 4's are first-mortgage bonds which draw upon earnings before the payments into the capital fund are required, i. e., between the levels of $139,089 and $1,694,041, and thus their earnings position, and, as shown above, their lien position, excels that of the old bonds, it is our view that the holders of the first-trust 4's are adequately compensated, through the allocation of securities provided for in the plan, for any rights surrendered as a result of such exchange.

The Rio Grande Junction bonds bore a coupon rate of 5 percent, but matured in 1939. They were not callable and are secured by a first lien on 62 miles of railroad, the debt secured amounting to $44,489 per mile. The loss-of-earnings position of these bonds and the off-setting features are almost identical with those of the first-trust 4's described above, although there is a slight difference in the percentage of new securities allocable. We conclude that the holders of these bonds are adequately compensated for the rights surrendered.

The petitions for intervention and further hearing filed by George A. Gaston, and referred to at the beginning of this report as having been denied, sought a determination of certain rights as to rental due for the Junction line and as to additions and betterments made thereon, in the light of the lease of 1889 and the supplemental agreements entered into by the Junction and the debtor as of December 1924. The petitioner's purpose was to request that, to the extent that we consider we are without jurisdiction to determine such rights, by reason of the fact that the Junction has not filed a petition under section 77, we should provide in the plan that the treatment accorded the Junction bondholders shall be without prejudice to their rights for rent during the period of the lease, and for an accounting of the earnings of the Junction.

The record contains much testimony and discussion relating to the Junction lease and the question of which system mortgage has a lien on the leasehold. We considered these matters in connection with our examination of the original segregation formula, and, regarding the modification of the lease, we expressed an opinion that there was no merit in the contention of the refunding and improvement mortgage trustee that the supplemental agreements, along with the transactions which followed their execution, were void. 233 I. C. C. 515, 570. Pending a final determination of the question by the court, we think that a further hearing and the presentation of additional evidence before us in behalf of the Junction bondholders would serve no useful purpose. Nor do we think it necessary to provide in the plan that the treatment accorded the Junction bonds is without prejudice to the rights of the bondholders for rent during the period of the lease. The claim, as established on the record before us, will be satisfied by the allotment of new securities shown in the plan.

As to the status of the Junction under section 77, we reviewed the facts in our second supplemental report, stating that we shall not attempt to adjudicate the question but shall provide for the inclusion of the Junction in the plan, with provision for its consolidation into the reorganized company. 254 I. C. C. 5, 27. The

accompanying order provides that four properties, including the Junction, shall be merged or consolidated to the extent legally possible, by transfer to the reorganized debtor or to a new company organized for the purpose.

The property of the Junction constitutes an unseparable part of the principal debtor's main line. Payments of interest on its bonds are in default. The debtor owns all of its stock, and the parties holding liens upon the stock and the lease are before us in this proceeding. The record is replete with evidence as to the earning power of the Junction. It is our view that public interest demands consolidation of the Junction with the reorganized company. In the light of the circumstances, we believe that the consolidation and the distribution of securities to the Junction bondholders should be upon a bankruptcy basis, under the provisions of section 77, and that the absence of the formality of the filing of the petition should not prevent such disposition of the matter.

In order to prevent failure of consummation of our entire plan, however, if there is delay in disposition of the Junction affairs, or to prevent holding up the plan pending extended reorganization proceedings for that company, the plan will provide that, in the event it appears to the judge that the consolidation of the Junction presents difficulties which may delay consummation of the plan with respect to the other debtor properties, the provisions for the Junction bondholders may be considered wholly separable, and the remainder of the plan consummated immediately. Under these circumstances, the Junction stock and lease would become assets of the reorganized company subject to the liens of its mortgages with provision for release in the event the consolidation is carried out, and the plan will provide for disaffirmance of the Junction lease in the discretion of the reorganization managers of the principal debtor and the judge.

The bonds issued under the Denver & Rio Grande consolidated mortgage, the so-called Eastern Consols, are not callable, and constitute a first lien on 1,553 miles of the main line of the debtor from Denver through Pueblo, Colo., to Rifle, Colo., and from Grand Junction, Colo., to Crevasse, Colo., the debt so secured amounting to $35,126 per mile. In addition, the mortgage is secured by a lien on 151 locomotives, 2,189 freight-train cars, 115 passenger-train cars and 482 units of work equipment. The rate-making value of all of this property indicated by the data of record is approximately $63,543,069, or nearly one-half the total for the system.

New first-mortgage bonds would, under the plan, be exchanged for 23.8 percent of the claim of the Eastern Consols, new income-

mortgage bonds for 16.2 percent, new preferred stock for 24 percent, and new common stock for 36.0 percent, of such claim. The new first and second mortgages would, in the case of consolidation, have liens as described above.

The Eastern Consols bore interest at the rates of 4 percent and 4½ percent, and matured in 1936. They did not have the benefit of any sinking fund. While they were entitled to payment of interest out of earnings between the approximate levels of $445,932 and $2,863,922, the securities allotted in exchange would be serviced from earnings at various levels in excess of $139,089 through the levels necessary to pay dividends on common stock. This apparent change in earnings position is offset by the new sinking fund and capital fund and by the increased rate of return obtainable from the new securities, i. e., slightly in excess of 4.5 percent for 64 percent of the claim and unlimited stock dividends for the remainder. Convertibility of the preferred stock into common stock serves also to compensate for change in earnings position and for surrender of lien and right to fixed interest with respect to 60 percent of the claim.

From a consideration of the foregoing and all other features of the plan, we conclude that the holders of the Eastern Consols are adequately compensated for the rights surrendered by them.

The Rio Grande Western consolidated-mortgage 4-percent bonds, sometimes referred to as the Western Consols, will mature on April 1, 1949, and are callable at par. The property subject to the first lien of this mortgage consists of 265 miles of main-line railroad west of Crevasse, Colo., 45 locomotives, 592 freight-train cars, 23 passenger-train cars, 167 units of work equipment, and the entire capital stock of the Utah Fuel Company, 100,000 shares. The evidence indicates a rate-making value of approximately $7,797,448 for this property, other than the fuel-company stock. The debt secured by the first lien amounts to $27,212 per mile of road, excluding the equipment. Under the plan, the old bondholders would receive directly the ownership, or the proceeds, of the fuel-company stock.

The Western consolidated mortgage constitutes a second lien on the property upon which the Rio Grande Western first-trust 4's are a first lien. The total debt secured by the combined first and second liens amounts to approximately $59,000 per mile, exclusive of equipment and collateral security.

The Western Consols now participate, through payment of interest, in earnings between the levels of $2,863,922 and $3,522,922. The securities allotted to them under the plan, i. e., 20 percent in new income bonds, 73 percent in new preferred stock, and 7 per-

cent in common stock, would receive interest and dividends out of earnings after the level of $3,142,846 is reached. Loss in earnings position and surrender of other rights, in our opinion, are offset by the possibility of increased return permitted by the 4½-percent income bonds, 5-percent convertible preferred stock, unlimited dividends on common stock, and the other features of the plan.

The debtor's 5-percent refunding and improvement mortgage bonds outstanding in the hands of the public, due April 1, 1978, are callable at 102½, and a sinking fund is provided for any bonds issued for the acquisition of equipment. No sums have been set aside in the fund for any of the 5-percent bonds now outstanding. The 6-percent bonds mature on October 1, 1974, and are callable at 107½. No sinking fund is provided for them.

The property subject to the first lien of the mortgage consists of 128 miles of branch lines, 150 locomotives, 9,816 freight-train cars, 113 passenger-train cars, and 119 units of work equipment, all having a total rate-making value of approximately $12,121,243.

The property subject to the second lien of the R. & I. mortgage consists of 1,818 miles of road having an indicated rate-making value of $71,340,517, and that subject to the third lien consists of 412 miles of road having an indicated rate-making value of $27,958,647. Various securities are pledged under the mortgage, the most important of which are the stocks of the Junction and the terminal companies. The average debt per mile secured by this mortgage and all prior liens amounts to $48,578 per mile of railroad, exclusive of equipment.

The holders of these bonds are allotted, under the plan, 17.7 percent of their claims in new first-mortgage bonds, 11.3 percent in new 4½-percent income bonds, 22 percent in the new 5-percent convertible preferred stock, and 49 percent in new common stock. The liens of the new securities are set out above. The total return to the holders of the R. & I's. from their new first-mortgage bonds, income bonds, and preferred stock, at the earnings level of approximately $6,200,000 a year, will equal 64 percent of present total requirements at an earnings level of approximately $4,462,000. In order to cover the full amount of present interest requirements, dividends of approximately $2.64 a share on the new common stock would have to be paid, which would require total earnings of $7,139,674.

The total annual interest requirements of the old refunding and improvement bonds was $720,000. The total annual interest and dividends on the bonds and preferred stock allotted to them under the plan is $461,910. They also will receive whatever dividends may be paid on 97,706 shares of common stock. Only about 32 per-

cent of the total interest and dividends payable on the new securities would come out of earnings before the level of $4,506,979 is reached, at which all the interest on the old bonds would be payable. Under the plan, there is a surrender-of-earnings position of these bonds with respect to 66 percent of their old requirements, or $477,430.

But the annual requirements of the new sinking funds provided for in the plan, which in part cause the change in the income position of the bonds, are $277,297, all of which goes to retire debt and improve the position of the junior securities allotted in exchange of the old bonds. In addition, the maximum annual requirements of the capital fund, which further dilutes the income position of the new junior securities so allotted, but which will be used to improve the debtor's property, amount to $750,000. It is our view that the various features of the new securities and of the plan as a whole adequately compensate the holders of the old refunding and improvement bonds for the rights surrendered by them under the exchange of securities provided for in the plan.

The allotments of securities to the holders of bonds of the five issues just discussed remain the same whether or not the consolidation plan becomes effective. We are of the view and find that the compensation to the holders of these five issues of bonds would be adequate under the provisions of the plan approved to take effect in case there is no consolidation.

On the basis of consolidation, the Finance Corporation should receive, in full settlement of its claim as of the effective date of the plan, $5,200,000 of new first-mortgage bonds and $8,700,605 of new income bonds.

The foregoing allotments to the bond groups will be unchanged in the event consolidation is not effected. The treatment of the claim of the Finance Corporation in such event will be by placing in escrow the pledged securities, or the reorganization securities issuable against certain items thereof, in the manner provided in the plan of July 13, 1942.

Appropriate changes will be made in section K of the order where the amounts of the new allocations are now modified, as indicated above. The provisions for extending the Chase National Bank note will be modified only to show the revised amounts of each class of new securities allocable to the bonds pledged as collateral security on the basis of the allocations herein approved for bonds of the same classes, respectively, and also on the basis of the interest accrued on the pledged bonds to January 1, 1943. In lieu of the securities formerly shown as replacing the collateral now held by the Chase National Bank, the new securities will consist of

$1,524,076 of first-mortgage bonds, $972,998 of income bonds, $1,894,332 of preferred stock, and $4,219,194 (42,192 shares) of common stock.

Voting trust; future control.—The plan of July 13, 1942, made the following provision with respect to the voting rights of the new stock:

> The preferred stock and common stock shall have equal voting rights, each share being entitled to one vote for the election of directors and in all matters of proprietary interest.

The plan provides, further, that all the preferred stock and common stock shall be placed in a voting trust under a 10-year escrow agreement, under which the stock of either class may be sold, subject to our approval, and with the consent of the holders of two-thirds of the escrow receipts representing the preferred and common, respectively.

The parties to the joint petition suggest the following modification of the first of these provisions:

> The preferred stock shall be entitled to one vote per share on the matters specified in section F hereinabove and on all matters as to which a vote by it is required by law but shall not be entitled to any other voting power except as follows: Until regular dividends at the maximum rate borne by the preferred stock shall have been paid in the amount of the equivalent of six quarterly dividends on all outstanding preferred stock, and thereafter so long as there shall be any unpaid accumulated dividends on the preferred stock equal, in the aggregate, to the equivalent of six quarterly dividends or more, the holders of the preferred stock, voting as a class, shall be entitled to elect two directors of the reorganized company, and the holders of common stock, voting as a class, shall be entitled to elect the remaining directors, which shall constitute a majority of the board. If, after the holders of the preferred stock shall have ceased to be entitled to elect directors (a) the reorganized company shall fail for 18 consecutive calendar months to pay full dividends on all preferred stock at the time outstanding or (b) accumulated unpaid dividends on the preferred stock of any series shall amount to the equivalent of six quarterly dividends or more, the holders of the preferred stock shall again be entitled to elect two directors until full current dividends shall have been paid on the preferred stock for the equivalent of six quarterly dividends and all dividends accumulated up to the end of the last preceding calendar year shall have been paid.
>
> The common stock shall be entitled to one vote per share.

The petitioners also suggest that the new preferred stock should be taken out of the proposed voting trust, with appropriate changes in sections I and M of our order.

In support of these proposals, the petitioners contend that the inclusion of the preferred stock in the escrow arrangement is unnecessary either to protect the continuity of management or to facilitate a sale of control to connecting lines. The number of shares of common stock outnumber the shares of preferred. It is

asserted that, if the common stock is voted as a unit, the preferred has no effective voting power except in such specific matters as to which the plan may confer the privilege of a separate class vote; that inclusion of the common stock, only, in the escrow arrangement would suffice both for continuity of management and for sale of control; inclusion of the preferred would actually obstruct the sale objective, if the plan means that the preferred, or some of it, must be sold if any stock is sold. If the preferred is issued for the purpose, among other purposes, of increasing as much as possible the market realization of the creditors receiving it, such creditors should not be compelled to leave such stock subject to the escrow provision, but should receive marketable certificates for the shares themselves. It is argued that, except for its special privilege of a class vote on specified corporate matters, the voting position of the preferred may be illusory and that it may be better protected by an assured power to obtain representation upon the board of directors upon default in its dividend payment than by a universal paper right of equal vote which might never procure any represenation; that the suggested change, so long as the representation is restricted to a minority of the board, might also improve the marketability of the common stock for sale to connecting roads. It is stated that the voting characteristics proposed are consistent with the listing policies of the New York Stock Exchange.

The restricted voting power suggested for the new preferred stock would be a distinct departure from the usual rule of equal voting rights per share for each class of stock issued. In several reorganization plans which we have approved, holders of the preferred stock are given the right to elect a majority of the boards of directors in the event preferred dividends at the maximum prescribed rate are not paid during 3 consecutive years. *Chicago, M., St. P. & P. R. Co. Reorganization*, 240 I. C. C. 257, *Chicago, R. I. & P. Ry. Co. Reorganization*, 247 I. C. C. 533, and *St. Louis S. W. Ry. Co. Reorganization*, 252 I. C. C. 325. A similar provision was proposed by the insurance-group committee itself under a suggested plan which accompanied the petition for modification of our plan of July 11, 1939, in this proceeding. At the same time, the committee was in favor of placing both the preferred stock and common stock in the voting trust, although the voting trustees were to be authorized to sell only the common.

The present joint proposal seems to be in line with that of the Missouri Pacific trustee, concurred in by the six chambers of commerce which filed a petition for modification of the plan, requesting an opportunity to acquire 50 percent of the voting control of the new company, where the control would be vested in the com-

mon stock. This matter was discussed in each of our previous reports, and it is still our view that the new owners of the property should decide what affiliations with other systems will be most advantageous. The plan for the voting trust was adopted in order to facilitate a possible sale of the new stock. It is also our view, as has been expressed in numerous cases, that the holders of preferred stock should have the same basic voting rights as the common, that is, one vote for each share in the election of directors and in all matters of proprietary interest. The question of marketability of the stock and the other considerations mentioned in the joint petition do not justify any departure from the rule. Accordingly, the proposal to limit the voting power of the preferred stock as described is disapproved, and no change will be made in the provisions for the voting trust.

In order to insure compliance with the listing requirements of the New York Stock Exchange under any future circumstances and also to permit cumulative voting, we deem it desirable to add a provision to the part of the order quoted above so that this part will read in full as follows:

> The preferred stock and common stock shall have equal voting rights, each share being entitled to one vote in the election of directors and in all matters of proprietary interest; provided, however, that the holders of the preferred stock, voting as a class, shall always have the right to elect not less than one-third, and in no event less than two, of the members of the board of directors. Cumulative voting shall be permitted.

Treatment of Finance Corporation claim.—The Finance Corporation considers the treatment of its claim under the plan of July 13, 1942, to be unfair and wholly inequitable and asks that the allocations be "substantially increased." Specific objections are made, in connection with the modified segregation formula, to the proportion of system earnings in 1935–40, which were allocated to the cut-off operation, to our alleged failure to allow for the profits of the lines west of Dotsero derived from traffic attracted by the cut-off, and to the alleged omission of the savings to be effected by consolidation. In connection with the final adjustment of the formula results (shown in tabular form in former appendix C) the Finance Corporation contended that consideration should have been given to the value of its second lien on the collateral pledged with the Chase National Bank and the Railroad Credit Corporation,[4] that the allotment of new first-mortgage bonds in the court plan was inadequate and should not have been followed, and that our analysis of the collateral pledged with the Finance Corporation

[4] As has been stated, the claim of the Railroad Credit Corporation has been paid.

on the basis of new securities assignable thereto was improper in at least two respects.

The debtor's segregation formula, based on operations during the so-called test period, namely, the 12 months ended June 30, 1935, showed the Denver's income available for interest to be $3,001,663, of which approximately 12 percent represented the earnings from the cut-off operation. Although, as we stated in our prior report, the record contains no analysis of the earnings of a later period, developed in the same way, we considered that the operating results during the period 1935–40 should be substituted for the test-period year in the formula calculations. As to the division of the earnings between the cut-off and the Denver's other operation in the 1935–40 period, we stated that the ratio of overhead freight tonnage moving via Denver to the Denver's total freight increased from 6.5 percent in 1935 to 9.1 percent in 1939, but we concluded that the original 12-percent division of the available income should be retained. At the court hearing in 1940, the Finance Corporation presented a study of the earnings from the cut-off operation in 1939, showing allocated gross revenues of $2,403,983 and earnings available for interest of $162,593. On this basis, the cut-off revenues were 11.1 percent of system revenues, but the available income was only 7.1 percent. At the court hearings in October 1942, and April 1943, witnesses testified that the proportion of system revenues contributed by the cut-off operation ranged from 25 percent in 1937 to 33.8 percent in 1942. It cannot be assumed from an increase in the ratio of tonnage that the income available for interest would change in the same proportion, as the Finance Corporation suggests. The tonnage figures may be regarded merely as an indication that the earnings of the cut-off operation in 1935–40 probably did not fall below 12 percent of the total, as established for the test period.

The Finance Corporation contends that the testimony indicates a profit of $1,300,000 in 1939, on the lines west of Dotsero, due to the cut-off traffic, and that neither the severance study nor the segregation study reflects this credit. In connection with the severance study, it was pointed out by the witness that the western lines would handle the bridge traffic whether it moved over the cut-off or via Pueblo. In any event, as was stated in our prior report, the severance study was not given controlling weight in the allocations arrived at by us. In order to provide for the contributed earnings in question in connection with the debtor's segregation formula, which we have used with various adjustments, it would be necessary to determine the earnings of the western lines in the period 1935–40, which were derived from the bridge traffic, and

to estimate what portion of such earnings had been attracted by the cut-off route and would not have moved over the Pueblo route. The record does not permit a satisfactory solution of this question, nor do we consider it essential to a fair determination of the treatment of the Finance Corporation claim.

The operating savings to be effected by consolidation of the Salt Lake are reflected in the debtor's segregation formula by the inclusion of an estimated amount therefor and are given weight in the primary distribution of new securities.

At the hearing before the court in April 1943, the Finance Corporation introduced an analysis purporting to show that the debtor's earnings from the cut-off operation available for interest in the year 1941 amounted to $1,149,700 and the earnings in the 4 preceding years ranged between $236,352 and $683,263. Studies introduced by the committee showed a deficit of $163,425 from operation of the cut-off in 1941, and larger deficits in the 3 preceding years. For 1942, the Finance Corporation showed a profit of $3,567,035, and the committee, a profit of $1,348,881. The differences arise primarily from different allowances of a mileage arbitrary to place the cut-off on a comparable basis with the longer route via Pueblo. Similar studies were presented for the debtor's operation over the Junction line.

The basic formula, modified and adopted by us for the plan, and explained in our prior reports, reflected an arbitrary of 175 miles for the cut-off. Insofar as the test year of the formula is concerned, the expert witnesses for the Finance Corporation and the committee agree on the use of this arbitrary and the cut-off earnings of approximately $370,000 which were computed on that basis. Their differences for the later years result principally from the fact that the committee's witness scaled down the arbitrary to 56 miles in 1939 and thereafter, for reasons explained. He regards the 175-mile figure as applicable only to the test year.

These studies were primarily concerned with the profit or loss from operating the Salt Lake Western line, since the amount of the rental was in question before the court. But the analyses covered the entire operation between Denver and Dotsero, and, as has been indicated, produced widely varying results. Whichever of these results might be accepted in lieu of the figure originally used, no new basis was supplied for a determination of the corresponding earnings of the other divisions of the system. All classes of creditors would be affected by such a change.

The final adjustments which we made in the allocations calculated by the modified segregation formula (former appendix C) resulted in the allotment of $4,802,040 of first-mortgage bonds,

$6,983,568 of income bonds, and $1,591,601 of preferred stock to the Finance Corporation. The considerations upon which these adjustments were made were stated at some length. We showed that the court, in its suggested plan, allotted $4,312,853 of first-mortgage bonds and $8,540,931 of income bonds to the claim, stating specifically that the allotment of the first-mortgage bonds was intended to equal the loan for constructing the cut-off. We found that the total amount of new first-mortgage bonds allocable to the pledged securities, on the basis of the plan then under consideration, was approximately $4,650,000. We discussed the committee's severance study and stated our conclusions. We were still of the opinion that the cut-off traffic possibilities had not yet been fully realized, but it was our view that on the evidence presented it was impossible to find any value in the cut-off control in addition to that reflected in the allocations made. It is our view that the additional evidence presented at the recent court hearing cannot be considered as in conflict with our conclusions as reflected in our adjustment of the allocations calculated by the formula, nor do we consider that such evidence justifies any change in the basis of our allocations of securities.

The analysis of pledged collateral, if revised to the extent necessary to conform to the plan herein approved, shows that there would be allocable to the bonds of classes publicly held $1,566,846 of new first-mortgage bonds, $1,388,150 of income bonds, $3,181,757 of preferred stock, and $3,861,910 of common stock. These allocations are on the same basis as if the pledged bonds were in the hands of the public.[5] With the assignment of new securities to the other collateral on the same basis as in our prior report, the total amount of new first-mortgage bonds assigned is $4,898,346. The value of the Finance Corporation's equity in the refunding and improvement mortgage bonds pledged with the Chase National Bank is, in our opinion, approximately $272,000. If this sum be added to the above-stated determination of first-mortgage bonds, the total would be $5,170,000.

For the Salt Lake Western stock pledged with the Finance Corporation, we allotted $1,815,500 of new first-mortgage bonds, $907,750 of preferred stock, and $907,750 of common stock, deeming such a set-up representative of a reasonable capital structure for a railroad such as the Salt Lake Western. The Finance Corpora-

[5] This was also the case in the previous analysis. Confusion was evidently caused by the phrase appearing in the second paragraph on sheet 14 of our prior report reading, "reflected in the allocations shown just above," which should have read, "reflected in the allocations shown in the table below." In the present allocations, account was taken of the transfer of $662,000 of D. & R. G. Consols to the Finance Corporation as a result of discharge of the Railroad Credit Corporation claim.

tion attempts to show that the Salt Lake Western is entitled to a larger proportion of first-mortgage bonds on the ground that the adjusted-earnings distribution used by us showed an income of $277,922 available for interest for the Denver's cut-off operation, and that the interest requirements of the Salt Lake bonds were more than covered by the separate earnings of the Salt Lake. The argument is not convincing, since the available income of $277,922 applies to the entire operation over the Salt Lake Western and Salt Lake, and, if capitalized by bonds, these bonds would theoretically be spread over both of these lines, notwithstanding the fact that bonds are already outstanding on the Salt Lake and are serviced by the earnings of the Salt Lake. We see no reason to alter our opinion as to the assignment of $1,815,500 of first-mortgage bonds to the Salt Lake Western stock.

The court's allotment of first-mortgage bonds to the claim of the Finance Corporation cannot be disregarded on the ground that the court failed to state what consideration it gave to the pledged collateral. The court was in possession of all the facts in this connection and had heard the testimony and arguments presented by the committee and the Finance Corporation, especially with regard to the value of the cut-off to the system. On the basis of the amount of the loan for constructing the Salt Lake Western, with interest to January 1, 1943, the new first-mortgage bonds assignable to the Finance Corporation claim under the court plan would be $4,983,590. If the estimated value of the Finance Corporation's equity in the Chase Bank collateral be added, the total would be approximately $5,255,000.

In our report of July 13, 1942, we found from a consideration of the entire record that the Finance Corporation was entitled to $4,802,040 of the first-mortgage bonds issuable under the plan therein approved, where consolidation is effected. Apportionment of the bonds now available for distribution between the classes of creditors on the ratios used in our prior report would give to the Finance Corporation $5,101,522 of the new first-mortgage bonds.

From a consideration of all of the foregoing, we conclude that $5,200,000 of first-mortgage bonds should be allotted, in the case of consolidation, to the Finance Corporation for its claim.

In section K of the plan, it is provided that, in the absence of consolidation, specific amounts of new securities shall be issued in respect of the pledged bonds of the publicly held classes, and that these new securities, together with the remaining collateral, shall be deposited in escrow, and escrow receipts issued to the Finance Corporation. Under the plan, all or any part of the escrowed securities may be sold at the request of the Finance Corporation, sub-

ject to specified conditions, and any or all receipts from the deposited securities, whether from sale, dividends, or interest, shall be paid over to the Finance Corporation and credited, first, against the interest accrued on the claim, any excess to apply on reduction of the principal. Conditions were prescribed as to the right of the new company to purchase the stock of the Salt Lake or of the Salt Lake Western, and as to the disposition of any securities or cash remaining after the Finance Corporation claim shall have been discharged, or after the expiration of the escrow agreement.

It was provided, further, that the amount of the Finance Corporation claim shall be adjusted and reduced in the amount of the money value of any award to the Finance Corporation which the court shall make upon the claim of the trustee of the Salt Lake Western against the trustees of the debtor in respect of the rental of the Salt Lake Western, and interest shall accrue only upon the total claim as so reduced. This latter provision, as stated in section J of our order, also applied in the case of consolidation, with appropriate adjustment in the allotment of new securities.

The Finance Corporation stresses the fact that we have not definitely found that its claim is fully secured nor found the cash value of the pledged securities. It argues that, if we deem the claim not to be fully secured and the value of the collateral less than the amount of the claim, it is entitled to receive all the pledged securities outright. In this connection, objection is raised to the proposal to reduce the allotment of securities by the amount of any award which the court may make for the rental of the Salt Lake Western line. The Finance Corporation insists that its right, as pledgee of the Salt Lake Western stock, to compensation for use of this line constitutes an expense of administration which must be provided for; that, unless the claim is fully secured, it does not follow that the new securities allocated should be reduced by reason of the rental payment, whether or not consolidation with the Salt Lake is effected; and, that the Finance Corporation cannot properly be deprived of its right to resort to every item of its collateral until full satisfaction of its claim is reached.

As we stated in our first report herein (July 11, 1939, 233 I. C. C. 515) the treatment accorded the Finance Corporation in both the debtor's plan and the committee's plan recognized the claim as fully secured. The plan which we then approved was predicated on this generally accepted position of the Finance Corporation and on certain considerations beyond the estimated value of the securities under pledge, including the fact that the Finance Corporation, as pledgee of the stocks of the Salt Lake and Salt Lake Western, held

a veto power in the consolidation of the properties, which formed the basis of the plan.

As a result of the record made at the court hearing on the plan and the opinions rendered by the judge, we modified our first plan so that consolidation was no longer made a prerequisite in the reorganization. Additional evidence has been introduced as to the earnings of the cut-off operation and the Salt Lake separate operation. The results of the application of the formula on the basis of the present record support the conclusion that the claim of the Finance Corporation is not fully secured. The allocation of securities to the Finance Corporation is on the basis of its collateral. We conclude that the plan should be modified to provide that, in case consolidation is accomplished under its provisions, no adjustment should be made on account of payments on the rent claim, in the securities allotted to the Finance Corporation claim.

In the event consolidation is not to be carried out; our plan provided, in effect, that the Finance Corporation should receive the full benefit of all the pledged securities, to the extent necessary to discharge the claim. Under this arrangement the pledged securities, or a part of them, may ultimately be reduced to possession by the Finance Corporation. Clearly the claim and the face amount of any note evidencing the indebtedness should be reduced by the amount of any rental allowance. The plan should be modified accordingly. Section J of the former order and so much of section K as relates to the Finance Corporation will be modified and consolidated as new section J, reading as follows:

* * * * * * *

(This statement of the provision is omitted here as it is shown in full in the plan.)

Matters connected with consolidation of the Denver & Salt Lake properties.—The plan of July 13, 1942, provides that the proposal for modification of the Salt Lake income bonds be submitted to the bondholders in the form determined by the reorganization committee, which shall report the results to the court, and, if the holders of 90 percent or more of the income bonds accept the proposal within 90 days of its submission, the consolidation of the Salt Lake properties with the debtor's properties shall be carried out as provided in the plan. Under this arrangement, the plan would be certified to the court and, if approved by it, would be submitted to the Denver's creditors for vote before the proposal to modify the terms of the Salt Lake is submitted to the holders of those bonds. The parties to the joint petition contend that the Denver's creditors cannot know what they are voting for unless the holders of the

Salt Lake income bonds shall have voted first, and suggest that the plan be first submitted to them by this Commission, and that the papers submitting the plan to creditors of the debtor shall state whether or not the holders of 90 percent in aggregate principal amount of the income bonds have consented to the plan.

The petitioners further contended that, if the plan is not accepted by the holders of 90 percent of the income bonds, then the Salt Lake Western lease and the Salt Lake trackage agreement should be disaffirmed and rejected by the plan, or at least that the plan shall not be submitted to the creditors for acceptance or rejection until such creditors and other parties shall have been given time to apply to the court for disaffirmance of the lease and trackage agreement and obtain an adjudication thereon.

The language used in the joint petition seems to indicate an intention to have the general plan, rather than the specific proposal for modification of bonds, submitted to the Salt Lake bondholders before submission to the Denver's creditors. It is immaterial, however, which document is meant. Not only is the Salt Lake not in process of reorganization under section 77, and its security holders not entitled to vote on the plan, but the act confers no power on anyone to put in force a part of a plan before the plan is confirmed. The submission of the plan to the classes of creditors entitled to vote for its acceptance or rejection is necessary before it can be confirmed. An informal vote secured from the holders of the income bonds would, of course, have no validity in the proceedings, nor would it be binding on the bondholders.

While those voting on the plan will not know in advance what the action of the holders of the Salt Lake income bonds will be, they will be able readily to ascertain from the plan the effect upon their interests in either event. The liens of the new bonds and the structure of the new system, with and without the Salt Lake, are clearly stated. Even if there were practicable means of submitting the proposal to the Salt Lake income bondholders we are not convinced that the alternative provided for in the plan is unjust to the debtor's creditors. The request for this modification of plan is denied.

Request was made in the joint petition that, if consolidation is not effected, the Salt Lake Western lease and the Salt Lake trackage agreement be disaffirmed, on the ground that the lease is impracticable and inequitable and if not disaffirmed would impose an unenforceable obligation on the new company. The petitioners objected to the possible assertion of a claim against the new company because of this "vague, unworkable, and excessive" lease. Replies to these contentions were filed by the Finance Corporation

and the Moffat tunnel interests, and all aspects of the matter were considered. In view of the ruling by the district court, that the lease and the agreement should be affirmed, any further discussion is unnecessary here, and no change will be made in section O of our order.

The joint petition proposes, as an incident to the other modifications of plan, that it be made clear that the Salt Lake Western is included within the plan, even in the absence of consolidation, and it is suggested that the following provision be included in section C of our order:

> Both the debtor and the secondary debtor shall be included within the plan and discharged from all their present debts (except those herein expressly provided to remain undisturbed) whether or not consolidation is effected.

This suggestion appears to arise from doubt as to the inclusion of the Salt Lake Western when its stock is preserved (under the plan for escrowing the Finance Corporation collateral, if consolidation is not effected) despite the extinguishment of the debt claim which is senior to the stock, that is, the note representing the loan to the Salt Lake Western. The Finance Corporation states that in the event, and only in the event, the plan makes fair and equitable provision for its claim, it will be willing to have the Salt Lake Western included in the plan and its indebtedness discharged as proposed.

We are of the opinion that the deposit of the Finance Corporation collateral in escrow for the benefit of the Finance Corporation, to the extent necessary to discharge the claim in full, as our plan provides, constitutes a fair and equitable provision for the claim and a discharge of the debt to the Finance Corporation in the event of no consolidation. As stated in the plan, no actual consolidation of the Salt Lake and Salt Lake Western will take place if the required consent of the Salt Lake income bondholders is not obtained. We approve the insertion of a statement that the plan is applicable to the Salt Lake Western as well as the Denver. We do not deem it necessary to provide for the discharge from debts as that situation will result from the provisions of the statute.

Assumption of obligations under the Salt Lake mortgages.—The plan of July 13, 1942, provided that the new company, in the event of consolidation of the Salt Lake, should assume the obligation to pay fixed interest at 4 percent on the Salt Lake first-mortgage bonds outstanding and the annual interest, as modified, on the Salt Lake income bonds. The terms of the Salt Lake first mortgage provide that, in the event of consolidation, the corporation into which the company is merged shall expressly assume the due and punc-

tual payment of principal and interest of all bonds. The income mortgage provides that the new corporation shall pay in cash all unpaid cumulative interest on the bonds and shall expressly assume the payment of principal and interest.

In view of this situation and on our own motion, we shall modify the provision under section K of our order (the third paragraph from the end of that section) to read as follows:

> In the event of consolidation with the Salt Lake on the basis herein provided, the new company shall assume all the obligations under the two Salt Lake mortgages, as stated therein in case of a merger into any other company, including the assumption of the obligation with respect to the payment of the principal and interest of all bonds now outstanding, except as the terms of the Salt Lake income bonds shall be modified, as provided above. No additional bonds shall be issued under either of the Salt Lake mortgages. The new company shall also assume the present tunnel contract, and the trackage agreement shall be canceled.

We conclude:

1. That, upon the petitions filed, the report and order of this Commission dated July 13, 1942, approving a modified plan of reorganization for the debtor and the secondary debtor pursuant to section 77 of the Bankruptcy Act, as amended, should be further modified as herein specified, and that as thus further modified, the plan will meet the requirements of section 77 (b) and (e) of the act, will be compatible with the public interest, and should be approved.

2. That, except as the plan shall be so further modified, the petitions for its modification should be denied.

3. That, except as modified herein, the findings and conclusions stated in our report of July 13, 1942, should be reaffirmed.

An appropriate supplemental order will be entered.

MILLER, *Commissioner*, dissenting in part:

Although the total capitalization approved in this report is nearer to what I think is justified than that approved in our original report, 233 I. C. C. 515, due to changed conditions affecting this carrier since that decision, it is still in the neighborhood of 10 percent too high. Otherwise, my separate expression in the second supplemental report, 254 I. C. C. 5, is applicable here.

APPENDIX A

Approved modified plan on the basis of consolidation with the Denver & Salt Lake

	Claims as of Jan. 1, 1943	Undisturbed or extended	First-mortgage bonds, 3 percent fixed interest, 1 percent prior contingent interest		Income bonds, 4½ percent contingent interest		Preferred stock, 5 percent		Common stock, $100 par value	
			Percentage	Amount	Percentage	Amount	Percentage	Amount	Percentage	Amount
			Percent		*Percent*		*Percent*		*Percent*	
Equipment obligations	$5,736,000	$5,736,000								
Rio Grande Western first-trust 4's	20,000,800		73.5	$14,737,338	26.5	$5,313,462				
Rio Grande Western consolidated 4's	20,036,400				20	4,011,280	73	$14,641,172	7	$1,403,948
Rio Grande Junction first 5's	2,736,333		77	2,123,916	23	634,417				
Denver & Rio Grande consolidated 4's	53,727,500		23.8	10,883,945	16.2	7,407,855	24	10,974,600	36	16,461,000
Denver & Rio Grande consolidated 4½'s	8,823,115		23.8	2,099,903	16.2	1,429,343	24	2,117,548	36	3,176,321
Refunding and improvement 5's	16,950,000		17.7	3,000,150	11.3	1,915,150	22	3,729,000	49	8,305,500
Refunding and improvement 6's	2,990,000		17.7	529,230	11.3	337,870	22	657,800	49	1,465,100
General-mortgage 5's	43,549,155								10	4,354,816
Chase National Bank note [1]	2,156,456	2,156,456								
R. R. Credit Corporation note, paid May 17, 1943										
R. V. C. notes	13,900,695			5,300,000		8,700,695				
Unsecured claims, approximate	440,000	no equity								
Total, Denver & Rio Grande Western	183,161,366	7,978,456		38,573,680		29,759,184		32,120,120		35,167,585
Denver & Salt Lake Securities: [2]										
Stock held by public 4,111 shares [3]								411,100		
								32,531,220		

[1] New securities to be issued for pledge as collateral on Chase National Bank note extended. First-mortgage bonds, $1,534,076; income bonds, $972,998; preferred stock, $1,894,332, and common stock, $4,219,194.

[2] First mortgage 4's, $1,500,000, assumed as to principal and interest, and income 6's, $9,734,000, also assumed as to principal and interest.

[3] Assigned 4,111 shares of new preferred stock.

APPENDIX B

Approved modified plan without consolidation with the Denver & Salt Lake

	Claims as of Jan. 1, 1943	Undisturbed or extended	First-mortgage bonds, 3 percent fixed interest, 1 percent prior contingent interest		Income bonds, 4½ percent contingent interest		Preferred stock, 5 percent		Common stock, $100 par value	
			Percentage	Amount	Percentage	Amount	Percentage	Amount	Percentage	Amount
			Percent		*Percent*		*Percent*		*Percent*	
Equipment obligations	$5,758,000	$5,758,000								
Rio Grande Western first-trust 4's	20,050,800		73.5	$14,737,338	26.5	$5,313,462				
Rio Grand Western consolidated 4's	20,056,400				20.0	4,011,280	73	$14,641,172	7	$1,403,948
Rio Grande Junction first 5's	2,758,333		77.0	2,123,916	23.0	634,417				
Denver & Rio Grande consolidated 4's	45,727,500		23.8	10,883,145	16.2	7,407,855	24	10,974,600	36	16,461,900
Denver & Rio Grande consolidated 4½'s	8,823,115		23.8	2,099,901	16.2	1,429,345	24	2,117,548	36	3,176,321
Refunding and improvement 5's	16,950,000		17.7	3,000,150	11.3	1,915,350	22	3,729,000	49	8,305,500
Refunding and improvement 6's	2,990,000		17.7	529,230	11.3	337,870	22	657,800	49	1,465,100
General-mortgage 5's	43,548,155								10	4,354,816
Chase National Bank note [1]	2,158,458	2,158,458								
R. R. Credit Corporation notes, paid May 17, 1943										
R. F. C. notes [1]	13,900,605	[2] 13,900,605								
Unsecured claims, approximate	440,000	no equity								
Total, Denver & Rio Grande Western	183,161,366	21,817,063		33,373,680		21,049,579		32,120,120		35,167,585
Denver & Salt Lake securities:										
Stock held by public, 4,111 shares, undisturbed										
First mortgage 4's		1,500,000 (undisturbed)								
Income 6's, including $1,266,000 held by R. F. C.		11,000,000 (undisturbed)								

[1] New securities to be issued for pledge as collateral, Chase National Bank note, extended: First-mortgage bonds, $1,524,076; income bonds, $972,998; preferred stock, $1,894,332; and common stock, $4,219,194.

[2] Note: R. F. C. claim to be provided for by depositing the pledged securities in escrow for a specified period, the receipts from sales, dividends and interest to be applied first to the payment of interest on the claim of $13,900,605 at 4 percent per annum, any excess to be applied to reduction of principal. For complete details see plan.

New securities to be nominally issued to R. F. C. in respect of its collateral of classes publicly held

	First-mortgage bonds	Income bonds	Preferred stock	Common stock
D. & R. G. consolidated 4's	$460,839	$313,681	$464,712	$697,068
R. G. W. first trust 4's	9,702	3,498		
R. G. W. consolidated 4's		371,070	1,354,406	129,874
Refunding and improvement 5's	1,096,305	699,901	1,362,639	3,034,968
Total	1,566,846	1,388,150	3,181,757	3,861,910

APPENDIX C

Capitalization and annual charges (see note below)

	On basis of consolidation with Denver & Salt Lake		Denver & Rio Grande Western without Denver & Salt Lake	
	Principal	Annual charges	Principal	Annual charges
Equipment-trust obligations	$5,758,000	$139,989	$5,758,000	$139,989
Chase National Bank note	2,158,458	[1] 45,722	2,158,458	[1] 45,722
R. F. C. claim (see plan)			13,900,605	[2] 556,024
Denver & Salt Lake first-mortgage bonds, 4 percent interest	1,500,000	60,000		
Denver & Salt Lake income bonds, 3-1 percent interest	9,734,000	292,020		
	19,150,458	537,731	21,817,063	741,735
New first-mortgage bonds, 3-1 percent interest	38,573,680	1,157,210	33,373,680	1,001,210
Total fixed interest	57,724,138	1,694,941	55,190,743	1,742,945
Capital fund, maximum payment		750,000		750,000
Prior contingent interest, 1 percent		[3] 498,318		[4] 348,978
Sinking fund for first-mortgage bonds, one half of 1 percent		[5] 200,189		[5] 182,323
		3,143,748		3,034,246
New income bonds, 4½ percent	29,750,184	[6] 1,364,133	21,049,579	[7] 972,606
Sinking fund for income bonds, one-fourth of 1 percent		[5] 76,808		[5] 58,527
Total debt, interest, payments to funds	87,474,322	4,584,689	76,240,322	4,055,379
New 5-percent preferred stock, par value $100	32,531,220	1,626,561	32,120,120	1,606,006
New common stock, par value $100	35,167,585		35,167,585	
Total capitalization	155,173,127		143,528,027	

[1] Fixed interest on the $1,524,076 of new first-mortgage bonds assigned as part of the collateral for new note to Chase National Bank.

[2] Payable only out of the proceeds of the escrowed securities, and not an obligation of the new company, as explained in the plan.

[3] Comprising prior contingent interest on:

New First-mortgage bonds $38,573,680	$385,737
New first-mortgage bonds assigned as part of collateral for new note to Chase National Bank, $1,524,076	15,241
Denver & Salt Lake income bonds	97,340
Total	498,318

[4] Comprising prior contingent interest on:

New first-mortgage bonds, $33,373,680	$333,737
New first-mortgage bonds assigned as part of collateral for new note to Chase National Bank	15,241
Total	348,978

[5] Including bonds to be nominally issued for pledge.

[6] Comprising contingent interest on:

New income bonds, $29,750,184	$1,338,758
New income bonds assigned as part of collateral for new note to Chase National Bank (only so much as necessary to fill out 4-percent interest on the note)	25,375
Total	1,364,133

[7] Comprising contingent interest on:

New income bonds, $21,049,579	$947,231
Part of interest on new income bonds assigned to Chase National Bank note, as in footnote 6	25,375
Total	972,606

NOTE.—The above statement does not purport to include the obligation or charges incurred through the new equipment program begun late in 1942 to facilitate the handling of traffic connected with military establishments and plants. See the accompanying report for details as to this program, new tax requirements, et cetera.

Distribution of new securities per $1,000 of present bonds with accrued interest

	First-mortgage bonds	Income bonds	Preferred stock	Common stock
Rio Grande Western first trusts ($15,190,000)	$970.20	$349.80		
Rio Grande Western consolidated's ($15,680,000)		266.00	$970.90	$93.10
Junction firsts ($2,000,000)	1,061.96	317.21		
Denver & Rio Grande consolidated 4's ($34,125,000)	318.92	217.08	321.60	482.40
Denver & Rio Grande consolidated 4½'s ($6,382,000)	329.03	223.97	331.80	497.70
Refunding and improvement 5's ($12,000,000)	250.01	159.81	310.75	692.13
Refunding and improvement 6's ($2,000,000)	294.61	168.94	328.90	732.55
General 5's ($29,808,000)				146.10

APPENDIX D

Development of new allocations on basis of consolidated system

	Claims as of Jan. 1, 1943	New first-mortgage bonds					New income bonds				Preferred stock	Common stock
		Formula distribution	Distribution of R. F. C. excess of $2,620,250		New allocations		Formula distribution	Deduct for foregoing increases in first-mortgage bonds	New allocations			
			Earnings		Bonds	Approximate	Final			Approximate	Final		
			Amount	Percent									
Rio Grande Western first-trust 4's	$20,050,800	13,634,544 (68%)	$866,190	43.2	$1,131,948	$14,766,492	$14,737,338 (73.5%)	$6,416,256 (32%)	$1,131,948	$5,284,308	$5,313,462 (26.5%)		
Rio Grande Western consolidated 4's	20,056,400							4,011,280 (20%)			4,011,280 (20%)	$14,641,172 (73%)	$1,403,948 (7%)
Junction first 5's	2,758,333	1,958,416 (71%)	126,362	6.3	165,076	2,123,492	2,123,916 (77.0%)	799,917 (29%)	165,076	634,841	634,417 (23.0%)		
Denver & Rio Grande consolidated 4's	45,727,500	10,090,950 (22%)	754,995	37.7	828,101	10,588,151	10,883,145 (23.8%)	8,239,950 (18%)	828,101	7,402,849	7,407,855 (16.2%)	10,974,600 (24%)	16,461,900 (36%)
Denver & Rio Grande consolidated 4½'s	8,823,115	1,941,085 (22%)			159,733	2,100,818	2,099,301 (23.8%)	1,588,161 (18%)	159,733	1,428,428	1,429,945 (16.2%)	2,117,548 (24%)	3,176,321 (36%)
Refunding and improvement 5's	16,950,000	2,712,000 (16%)	236,880	12.8	285,083	2,997,083	3,000,150 (17.7%)	2,203,300 (13%)	285,083	1,918,412	1,915,350 (11.3%)	3,729,000 (22%)	8,305,500 (49%)
Refunding and improvement 6's	2,990,000	478,400 (16%)			50,309	528,709	529,230 (17.7%)	388,700 (13%)	50,309	338,391	337,870 (11.3%)	657,800 (22%)	1,465,100 (49%)
Subtotal				100.0	2,620,250				2,620,250				
General mortgage 5's	33,548,155												4,354,816 (10%)
R. F. C. claim	13,900,605	7,820,220 (56%)			2,620,250		5,200,000	6,165,342 (44%)	2,620,250	3,785,582	8,703,605		
Total							38,573,680				29,750,184	32,120,120	35,167,585

United States District Court

DISTRICT OF COLORADO

Filed Oct. 25, 1943.
G. WALTER BOWMAN,
Clerk.

In the Matter of
THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, *Debtor.* } No. 8669

OPINION
APPROVING PLAN OF REORGANIZATION

The Denver and Rio Grande Western Railroad Company, as debtor, and the Denver and Salt Lake Western Railroad Company, as secondary debtor, filed November 1, 1935, petitions in this court alleging they were unable to pay their debts as they matured, and desired to effect a plan of reorganization under §77 of the Act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States," as amended. On the same day the petitions were filed the court entered orders approving the petitions as properly filed, and authorized and directed the debtor to operate and maintain both properties under the supervision of the court.

On November 18, 1935, Wilson McCarthy and Henry Swan were appointed Trustees for the debtor. These appointments were ratified by Division 4 of the Interstate Commerce Commission. On December 18, 1935, the court appointed Raymond L. Sauter, Trustee of the secondary debtor, The Denver and Salt Lake Western Railroad Company. This appointment was ratified by the Interstate Commerce Commission. He resigned April 21, 1941 and H. Allyn Hicks, Jr., was appointed as his successor June 13, 1941. April 29, 1936, upon petition of the debtor, an order was made extending the time for filing a plan of reorganization under §77 (d) to and including August 1, 1936. On July 29, 1936, a proposed plan of consolidation and reorganization, as of January 1, 1937, was filed with the court and the Interstate Commerce Commission by the debtor. This plan included the Denver and Rio Grande Western, the Salt Lake Western, the Denver and Salt Lake Railway Company (the Moffat Road), the Rio Grande Junction Railway Company, and the Goshen Valley Railroad Company.

Public hearings on the plan began and were held before the Interstate Commerce Commission in October, 1936, and in February, April, and June, 1937. On June 15, 1937, a plan of reorganization, including the companies covered by the debtor's plan, was filed by the so-called "Insurance Group Committee," intervener, of which George S. Van Schaick was chairman. In addition to this group other intervenors included the trustees under certain mortgages, the Security Research Bureau, the Untermyer family, Chase National Bank of New York, the Railroad Credit Corporation, various chambers of commerce and boards of trade, the Reconstruction Finance Corporation and others.

By report and order of July 11, 1939, (233 I. C. C. 515) the Commission approved a plan of reorganization for the Denver and Rio Grande Western Railroad Company and the Denver and Salt Lake Western Railroad Company, secondary debtor, The Denver and Salt Lake Railway Company, the Rio Grande Junction Railway Company and the Goshen Valley Railroad Company. Thereafter, on September 1, 1939, petitions for modification of the approved plan were filed by the so-called Insurance Group Committee, by Guy A. Thompson, Trustee of the Missouri Pacific Railroad Company, and many other interested parties.

Thereafter the Commission, having reconsidered its prior report and order, came to the conclusion that certain provisions of the plan should be modified and certain other provisions, as to which some question had been raised, should be retained without change. And on April 2, 1940, the Commission entered an order setting forth and approving a modified plan of reorganization for the Denver and Rio Grande Western Railroad Company and the Denver and Salt Lake Western Railroad Company, effective June 30, 1938, and revoking and superseding the order of July 11, 1939 (239 I. C. C. 583).

This order having been certified and filed in the court on April 11, 1940, on May 6, 1940 it was ordered all parties in interest file their objections to the plan of the Commission and their claims, if any, for equitable treatment on or before July 1, 1940, and set said objections and claims for equitable treatment for hearing on Monday, July 29, 1940.

Accordingly the matter came before this court July 29, 1940, for hearing upon the specific written objections to the plan and claims for equitable treatment (Tit. 11, §205, subdivision (e), U. S. C. A.). Testimony was taken up to August 12, 1940, at the conclusion of which, and before argument, at the suggestion of counsel, an informal conference with counsel was held in the court chambers, and at the request of counsel the court indicated

its views as to certain features for a proper plan of reorganization. (see interim memorandum of August 30, 1940), stating therein that any plan approved by the court should be within the framework of the Interstate Commerce Commission plan; that it strongly favored the consolidation of the Salt Lake and the Denver—which all the testimony supported—and setting out other requirements of any plan the court would approve, and emphasizing that the amount of fixed charges in any plan the court would approve was that fixed by the Interstate Commerce Commission, to wit, $29,403,144 of fixed interest first mortgage bonds, total fixed charges $1,278,539.

As to the allocation of the first mortgage bonds, the court indicated the three divisional mortgages, i. e., Rio Grande Western First Trust 4s, Rio Grande Junction First 5s and part of the Denver and Rio Grande Consolidated 4s and 4½s,

> "should share in the new fixed interest first mortgage bonds with the Reconstruction Finance Corporation notes on such a proportional basis as the Rio Grande Junction rate of bonded indebtedness per mile for each of such mileage, thereby awarding new fixed interest first mortgage 4s to these three divisional first mortgages, and to the Reconstruction Finance Corporation notes."

This allocation of first mortgage bonds, differing from the Interstate Commerce Commission plan, was based on traffic density between Dotsero and Salt Lake City. It is recognized that the Rio Grande Junction 5s cover sixty miles of track running from Rifle to Grand Junction, which produces substantially no local business, and the system could afford, if necessary, to turn it over to its bondholders and duplicate this mileage with a better and straighter line at a cost of less than $3,000,000. In addition, the mileage between Dotsero and Salt Lake City covered by these mortgages is dependent upon the system as a whole for equipment, terminal facilities, shops and overhead organization and personnel.

After the hearing on the Commission's report and order of April 2, 1940, above referred to, and on March 6, 1941, the court filed its opinion disapproving the Commission's plan largely for the reasons just stated, and on the same date entered its order referring the proceedings back to the Commission under Section 77 (e). In its opinion the court suggested a plan which became known as the "Court Plan." Thereafter further hearings occurred before the Commission and on July 13, 1942, it promulgated its second supplemental report and order wherein it, in effect, revoked its prior orders and substituted its said second supplemental report and

order (254 I. C. C. 5). To this, various petitions for modifications were filed with the Commission, and on June 14, 1943, it promulgated its third supplemental report and order further modifying its prior order of July 13, 1942, and as so modified, approving the same (254 I. C. C. 349).

The matter is now before the court for approval or disapproval of the Commission's plan culminating in its said third supplemental report and order of June 14, 1943, modifying its prior reports and orders. Reference to the hearing thereon before the court will be made later herein.

Railroad transportation has been a sick industry. Whether the capital burden imposed upon them has played a causative role in their maladies, or has become excessive only by reason of weakness induced by other causes, it is clear that many carriers can face the competition and other hazards of the future only if their capital charges are drastically reduced. For many, therefore, reorganization on a considerable scale was long ago indicated. Thirty per cent of the mileage of American railroads has already been subject to this process.

When most of the railroads were built—preceding 1850—financing was usually accomplished by sale of capital stock—rarely by mortgage. Underestimation of original cost was the chief source of later financial difficulties. This led to the use of the corporate mortgage necessary to finish construction, and in the era following 1850 the law and technique of corporate reorganization had its real beginning and the mortgage was used with an increasingly lavish hand. This led to the modern equity reorganization, involving the foreclosure and sale of the carrier's property to a new company formed to take it over.

Sec. 77 of the New Bankruptcy Act provides for the reorganization in the Federal courts of insolvent interstate railroads unable to meet their debts as they matured. An elaborate procedure is set out in the statute. The new statute was designed to provide a method to avoid the undue delay and inordinate costs incident to the old equity reorganization, and adoption of a fair, equitable and financially sound plan, surrounded by administrative and judicial safeguards, thought to be lacking in the equity process.

No plan can become effective without the prior approval of the Interstate Commerce Commission and the court, and they must first make a finding it is equitable, does not discriminate unfairly in favor of any class of creditors or stockholders, is financially feasible, and in the public interest. The plan must be accepted by two-thirds majority of any class of creditors or stockholders before it becomes binding upon the remainder of the class. It further

provides that the consent of any class of creditors or stockholders could be dispensed with where (1), the plan provided for the payment in cash of the value of the claim, or the value of the securities allocated under the plan to any interest in the old company. Or (2), where provision was made in the reorganization plan for a sale of the debtor's property to the reorganized company at a price not less than that to be fixed by the Interstate Commerce Commission (§77b). Shareholder approval can also be dispensed with, where it is established that their equity in the enterprise is gone. And bondholders' acceptance is unnecessary where the reorganization plan provided for the sale of the debtor's property, subject to their liens. Sec. 77 (e) of the Bankruptcy Act (Tit. 11, U. S. C. A., §205).

The amendments of 1935, while changing almost the entire language, retained the underlying concepts of §77. By it stockholders' consent is made unnecessary where the company is found to be insolvent; that is, where the value of its assets was less than its total debts. The Commission, as well as this court, has on several occasions found—and the court now finds—that the debtor is insolvent and there is no equity to justify the issuance of any securities to the stockholders of the debtor. And it is further provided that readjustment may become binding on the dissenting classes of creditors and stockholders in the event the court finds after a hearing that the plan makes provision for appraisal of their interests and cash payment of the value thereof. And where the court finds after hearing that the plan makes adequate provision for objectors' interests, their rejection of the approved plan of securities readjustment is not reasonably justified.

This railroad reorganization process of §77 has, over many years, accomplished a long step towards sound, fair, and equitable reorganizations. Like all new legislation, however, experience has developed some deficiencies. Out of the many controversies over the Act and its meaning it has been made clear that a §77 reorganization must meet the requirements of the *Boyd case*, 288 U. S. 482. In three recent cases, *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523, and *Los Angeles Lumber Products Co.*, 308 U. S. 106, the Supreme Court has cleared up many disputed questions.

A reading of these cases forces the conclusion that the drafting and formulation of a sound reorganization plan is a most difficult job, especially when, as here, there are overlapping divisional mortgages and liens. It is well to observe that in twelve out of the first eighteen reorganizations before the Commission that have reached final report the common stock was found to be valueless.

In two, the Kansas, Kaw Valley & Western, and the debtor's amended plan of January 1, 1939 in the New Haven case, the debtor's plans themselves actually provided stockholders be given nothing.

Fixed charges can not be too high in relation to earning power. Neither can they be too low, because securities carrying a return which is not fixed, require a higher coupon rate. Earning power, as the Supreme Court has held *(supra)*, must obviously be the determining factor in arriving at the amount of securities the debtor can support. The main objective of a sound plan of reorganization is the determination of the future net earning power of the property and the amount of new securities such earnings will conservatively support over good and bad years alike.

For the last ten years the total consolidated net earnings available for interest on the Rio Grande and the Salt Lake—1933 to 1942, inclusive— were $43,157,877, 80% of which is $34,526,302—an average of $3,452,630 per year. This includes, of course, the inflated earnings for 1942 of $18,144,032—three times the net earnings for any single year of the ten. Comparing this with the fixed charges called for by the plan now before the court providing for total fixed charges of $1,694,941, compared with $1,766,966 called for in the 1942 plan, and $2,637,552 fixed charges provided for in the court plan of 1941. All this on the basis of consolidation with the Salt Lake. It would thus seem that on a conservative basis the prospective earnings determined as near as can be, justify the present plan.

As a commentary on the past reorganizations it is interesting to note that before the 1924 reorganization the total capitalization of the Denver and Rio Grande Western, including common and preferred stock, was $193,764,582, and at the conclusion of the reorganization the capitalization of the new company was $208,480,786—an increase rather than a decrease. With this experience the court, like a burned child, dreads the fire.

The *Western Pacific case (supra)*, held, 318 U. S. 472:

> "The power of the court does not extend to participation in all responsibilities of the Commission. Valuation is a function limited to the Commission, without the necessity of approval by the court." Sec. 77 (e), (Tit. 11, U. S. C. A., §205).

And:

> "The function of valuation thus left to the Commission is the determination of the worth of the property valued, whether stated in dollars, in securities or otherwise. * * *. None of the findings required of the judge under subsection (e) relate

specifically to valuation * * *. It leaves open the question of whether, in reaching the result the Commission had applied improper statutory standards."

The same case also held that the determination of whether the plan is "compatible with the public interest" (subsection (d) of §77 of the Bankruptcy Act (Tit. 11, U. S. C. A., §205), likewise rests with the Commission. This phrase includes, according to the Supreme Court, questions as to the amount and character of the capitalization, and 318 U. S. 474:

"So long as legal standards are followed, the judgment of the Commission on such capitalization is final."

The Supreme Court also held (syllabus No. 7):

"Section 77 (e) authorized the elimination from participation in the reorganization of stockholders and creditors whose claims are valueless."

And their elimination

"does not deprive such claimants of property without due process of law."

Further (syllabus No. 8), that nothing in the Act

"requires the issuance of warrants to stockholders and creditors whose claims, found to be without value, have been eliminated from participation in the reorganization."

And (syllabus No. 9):

"The mere possibility that earnings of the reorganized railroad may exceed expectations does not justify the issue of securities based upon such a possibility."

And further (syllabus No. 15):

"Sound railroad reorganization requires consideration of the interest of the public in an adequate, transportation system, properly financed, and this must be balanced against the satisfaction of claims, without equity, by the issue of securities without reasonable opportunities to earn a return."

Further, that a showing made before the district court as to changed conditions, to wit, increased earnings due to the war, forms no basis for rejection of the Commission's plan.

In this connection it should be stated in regard to inflated war earnings, that the passenger traffic on this property for the twelve months ending August 31, 1943 equaled $9,255,631, of which $5,536,307—or 59%—is the result of transportation of soldiers for the Government. This does not include soldiers traveling on fur-

lough or on personal account nor other passenger traffic directly due to the war such as the families of soldiers in the service going to and from camps or of representatives of Government departments incidental to the war.

Freight earnings for the 12 months ending August 31, 1943 were $57,702,824. It is difficult, if not impossible, to determine just what part of these freight earnings are due to the war effort. During the 12 months ending in August, total loadings and receipts from connections were 514,520 cars. This included 138,884 carloads consigned to various Government agencies, but does not include business moving to contractors doing Government work, nor to or from war industries operated independently, such as the so-called "Kaiser Operations," or the Colorado Fuel & Iron Company. The representatives of the Traffic Department estimate that between 60% and 70% of the present freight traffic is due to the war effort.

It would, therefore, seem that very little, if any, of these inflated earnings are sufficiently permanent to form a basis for additional securities.

In the *Milwaukee case (supra)*, the court (318 U. S. 536), sustained the Commission's conclusion that the equity of the holders of debtor's preferred and common stock was without value, and they were, therefore, not entitled to participate in the reorganization.

And (p. 541): If there was no reasonable probability that the earning power of the road would be sufficient to pay prior claims of interest and principal and leave some surplus for the service of stock, then the inclusion of stock would violate the full priority rule incorporated in §77 by the phrase "fair and equitable." Page 540: Earning power is the primary criterion of value in reorganization proceedings. Page 543: Earning power in war years is not a reliable criterion for the indefinite future. And (pp. 544 and 545): The nature of the capital structure, and the amount of the capitalization, is for the determination of the Commission, and all questions of ratio of debt to stock, the amount of fixed, as distinguished from contingent interest, and the kind of capital structure which a particular company may need to survive, are for the expert judgment of the Commission which the courts must respect. Page 566:

> "Whether in a given case senior creditors have been made whole or received 'full compensatory treatment' rests in the informed judgment of the Commission and the District Court on consideration of all relevant facts."

In *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106, it was held (p. 115), that creditors are entitled to absolute priority over stockholders against the property of an insolvent corporation —relative priority not being sufficient.

When the court took over the property on November 1, 1935, and appointed Trustees, the physical condition of the estate was very bad. The management, in order to pay past due interest on outstanding securities, had not only used funds that should have been devoted to proper maintenance, but had actually borrowed money from the Reconstruction Finance Corporation to pay interest on funded debt, and current taxes as well. As a result a great deal of deferred maintenance had been allowed to accumulate. It is hard to understand the policy of the Reconstruction Finance Corporation in loaning money to this debtor for such purposes and thereby postponing and making worse the inevitable bankruptcy. The road was in such shape that on many sections of the main line trains were run on "slow orders." There was lack of protection of the roadbed and bridges on streams adjacent thereto, the rolling stock was in bad shape, all motive power was in need of repair, and the shops lacked adequate equipment.

The Trustees promptly drew up an improvement program and prosecuted it at a cost through and including the first half of 1943 of roughly $40,000,000. This includes $1,065,000 for the installation of centralized traffic control on 115 miles of the main line—mostly west of Dotsero. The net result of this alone was to enable the road to give an operation efficiency on a single track equal to about 90% of what could have been accomplished on a double track operation. $104,000 was spent on automatic block signals on the Salt Lake Western between Bond and Dotsero, and new slag ballast installed on 413 miles of roadbed, and 436 miles of new rail was laid at a cost of $6,968,500. Main terminals and freight yards were enlarged and improved at a cost of over $1,700,000. In addition many line and grade changes were made, passing tracks installed at various points, and a considerable amount of roadway and work equipment acquired.

The rehabilitation of the equipment included the purchase of six Diesel freight locomotives at a cost of $3,018,928; 23 Diesel switching locomotives $1,450,318; 20 new steam locomotives $3,759,757. In addition the Trustees purchased eight second-hand locomotives, and have five additional locomotives on lease from Defense Corporation, and have on order six more Diesel freight locomotives for delivery early in 1944.

To handle properly the present volume of business offered, further additional equipment, including motive power is required,

which can not now be obtained. The economy of Diesel operation is recognized in railroad circles, and it is the prediction of operating officials that Diesel power will supplant steam on American Railways after the war as soon as the necessary equipment can be made available. It is especially adapted to railroads running through mountainous territory with heavy grades. In addition the Trustees purchased 100 ballast, 1902 box cars, 100 automobile box cars and 791 gondola cars, including coal cars. To finance these improvements the Trustees borrowed on Trustees Certificates. $7,245,000. The first issue of these Certificates—Series D—carried an interest rate of 3¼% and the last—Series I—were sold on a 2% basis. Of this amount $1,970,000 was paid at maturity, leaving $5,275,000 outstanding in September, 1943, which the Trustees have offered to pay off without success. In addition a debt of $2,687,689 incurred under conditional sale agreements has been paid off before maturity together with the note due the Railroad Credit Corporation in the amount of $261,847. Furthermore, Series A, B, and C Equipment Trust Certificates, amounting to $2,325,000 outstanding when the Trustees took over, have been paid off. These particular Equipment Trust Certificates bore an interest rate of from 4½% to 5½%, compared with the 2% rate on the Trustees' certificates. This indicates the greatly improved credit rating the property established in banking circles under Trusteeship.

These improvements—often made over the objections of the bondholders and creditors—were justified, for otherwise the property could not have begun to handle the increased volume of traffic resulting from the war effort. As an example, the average freight train speed on this road increased steadily until in 1941, for the first time, at least since 1920, the year's average speed on the Rio Grande was faster than the average for the nation's railroads as a whole. It has not been possible, however, to maintain this rapid service even with increased facilities, taxed as the system is under wartime conditions. Yet it is noteworthy that this property in 1943 is demonstrating its ability to produce more than twice as many gross ton miles as in 1929—the heaviest year prior to Trusteeship—with a train speed 20% faster than in that year.

The opening of the Dotsero Cutoff, saving 175 miles between Denver and Salt Lake and Ogden, and the improvements made during the Trusteeship, placed the property for the first time in a competitive position with other transcontinental carriers enabling it to participate in through business with schedules on a par with other transcontinental carriers.

No material change has been made in the 146-hour basic schedule established by the transcontinental lines for eastbound freight.

from the Coast to Chicago. This required the Rio Grande to move trains from Ogden to Denver and Pueblo in 30 hours and 17 minutes. As a result of the war and the request of the Office of Defense Transportation, in 1942 this eastbound schedule was lengthened 24 hours between California and Chicago, increasing the Rio Grande schedule to 35 hours 15 minutes. Prior to 1936 the agreed westbound freight schedule from Chicago to the Pacific Coast called for seventh morning delivery. The Rio Grande's part of this schedule was 35 hours from Pueblo to Ogden, and 35 hours from Denver to Ogden. In 1936 this westbound schedule was reduced to provide for a sixth morning delivery from Chicago. This required the Rio Grande to make the run from Denver to Ogden in 26 hours, and from Pueblo in 27 hours and 30 minutes. This schedule remained in effect until November, 1941, when it went back to the seventh morning delivery.

The road runs through mountainous territory and along many streams subject to periodic floods, and there is constant danger of falling rocks and slides. This hazard has necessitated the installation of protective measures against accidents resulting from rock on the track, etc., involving constant expenditure to maintain bridges and roadbeds through deep canons, where flood conditions regularly prevail during certain times of the year. For these reasons the hope is expressed that when the railroad is taken back by its owners that the balance of the Trustees' improvement work in these respects will be carried out.

The Moffat Tunnel and the Cutoff carry more than twice as much traffic as they were originally designed for, and central traffic control on that line is strongly indicated. Smoke conditions in the Tunnel are very bad and present a problem that must be solved in the near future, either by the exclusive use of Diesel engines or the installation of some form of electric power between Denver and Bond.

This recitation of the improvement in the condition of the property between the appointment of the Trustees and this hearing bears out the experience of the court with this property in four receiverships—two of the four under my incumbency as Judge. Each time the property has been taken over by the court in a very bad condition physically, with a large amount of deferred maintenance, lack of sufficient power and rolling stock, and each time it has left the court in A-1 condition, and capable of performing its duty as a public carrier.

The Rio Grande Railroad is the largest business enterprise in Colorado, and the largest taxpayer, and also gives a very large service to the State of Utah, and the hope is expressed that when

the property is returned to the security holders they will realize their responsibility as the owners of a public utility that contributes so much to the prosperity and well-being of the states and communities it serves. The losses they have suffered in these various reorganizations can be directly traced to the security holders' failure to recognize this responsibility, and their lack of interest in their investment and its management. They have tolerated a management of their property between recurring receiverships that has resulted in failure to make earnings sufficient to maintain the overcapitalized financial structures. Failure to realize this responsibility will inevitably result in a form of reorganization carried out by a bureau of the Government less sympathetic to the owners of the property, resulting in a far greater scaling down of the capital structure than is now required by §77.

The new management of the property should be made up of Western men familiar with the problems of the customers living in the territory served by the railroad. Its control as in the past should not be centered in a group of financial institutions in New York City, the officers of which have never willingly ventured west of the Hudson River, and who set foot for the first time on their property when invited on an inspection trip by the Trustees.

This proceeding has been pending in this court approximately eight years. As already stated, the Commission's plan of April 2, 1940, certified to the court, was rejected because of its failure to give due recognition to the Rio Grande Western First Trust 4s and the Junction 5s, as compared with the Reconstruction Finance Corporation notes; and the court at that time in referring the proceedings back to the Commission, outlined a plan embodying the court's views, dated March 6, 1941. The plan now before the court bears more resemblance to the court plan than to the one first put out by the Commission.

This plan was set for hearing before the court on September 13, 1943, pursuant to notice. On April 13, 1943, the court heard, upon notice to all parties, the petition of the Trustee of the Denver and Salt Lake Western, filed March 25, 1936, as amended April 27, 1936, for payment of rental and other amounts by the Denver and Rio Grande Western Railroad Company, and upon the supplemental petition for payment of rental for the Denver and Salt Lake Western Railroad Company properties, filed February 8, 1943, and the petition of the Moffat Tunnel Improvement District in support of said petitions of the Trustee of the Salt Lake Western.

The court, after hearing testimony and arguments entered its findings, order and decree on September 13, 1943, confirming the joint trackage agreement between the Denver and Salt Lake Rail-

way Company and the Rio Grande, dated October 15, 1928, and the Dotsero Cutoff agreement between the Denver and Salt Lake Railway Company, the Salt Lake Western, and the Denver and Rio Grande, dated June 22, 1931, as modified by a subsequent agreement between the Rio Grande and the Reconstruction Finance Corporation, fixing the rental as therein provided.

It was further ordered, pursuant to the findings made, that the Rio Grande or its Trustees were not obligated to pay the Salt Lake Western as rental for the use of the Dotsero Cutoff either the interest on the principal obligation of the Salt Lake Western or the Rio Grande under the so-called stock purchase loan agreement of December 19, 1934, any Federal or state income taxes, excess profit taxes or other taxes levied upon the income of the Salt Lake Western. And further ordered the Trustees of the debtor Rio Grande to perform and to continue to perform the obligations of the Rio Grande contained in said leases and agreements and pay the rent due to date with interest and in the future.

On June 23, 1943, the Central Hanover Bank and Trust Company, Trustee under the first mortgage of the Rio Grande Junction Railway Company, dated December 1, 1889, filed its petition dated June 14, 1943, asking the court to require the debtor to pay to the Rio Grande Junction Company, for application upon the Junction bonds the principal amount of said bonds, together with interest thereon, from June 1, 1935 to date. The matter was duly noticed for hearing on June 28, 1943, and on June 23, 1943, on motion for continuance, the hearing was by request and consent of all the parties in interest including the Chase National Bank of the City of New York, as Trustee under the Denver and Rio Grande Western Railroad Company Refunding and Improvement Mortgage, continued to meet the convenience of New York counsel until September 13, 1943.

After a discussion of the status of the Junction, the Commission said in its third supplemental report of June 14, 1943 (254 I. C. C. on 363):

> "In order to prevent failure of consummation of our entire plan, however, if there is delay in disposition of the Junction affairs, or to prevent holding up the plan pending extended reorganization proceedings for that company, the plan will provide that, in the event it appears to the judge that the consolidation of the Junction presents difficulties which may delay consummation of the plan with respect to the other debtor properties, the provisions for the Junction bondholders may be considered wholly separable, and the remainder of the

plan consummated immediately. Under these circumstances, the Junction stock and lease would become assets of the reorganized company subject to the liens of its mortgages with provision for release in the event the consolidation is carried out, and the plan will provide for disaffirmance of the Junction lease in the discretion of the reorganization managers of the principal debtor and the judge."

And substantially the same statement is contained in its order (254 I. C. C. on 386) which order also provides (254 I. C. C. on 404):

"* * * The construction of the plan by the court shall be final and conclusive. The court may cure any defect, supply any omission, or reconcile any inconsistency, in such manner or to such extent as may be necessary or expedient to carry out the plan effectively."

The Commission's plan allocates to holders of the Junction Company's First Mortgage Bonds 77% of their claim in first mortgage bonds on the reorganized company, and 23% in its income bonds. The outstanding problem with respect to the Junction is that it is not in trusteeship and the trustee under its First mortgage and certain bondholders have contended that the Commission had no power to allocate new securities in lieu of the first mortgage bonds or to compel acceptance thereof by the bondholders.

To the court solution of the problem seemed very simple. The trustees having on hand an amount of cash far in excess of the needs of the reorganization expenses, including working capital, and taking into account debtor's guaranty of the payment of the bonds with interest, considers the question as a matter of ordinary administration of the property, and having the old-fashioned, perhaps, feeling that this excess cash should be used to reduce indebtedness when possible, ordered the trustees to purchase the Junction bonds at 100% and interest, or pay them off, whichever seemed the most advantageous.

Accordingly and on September 16, 1943, the court entered an order directing the trustees to purchase the Junction bonds at par and accrued interest at 5% per annum, from June 1, 1935, from all bondholders tendering their bonds for purchase and the trustees have given notice pursuant to the order that on and after November 1, 1943, they will purchase such bonds at said price, but with accrued interest terminating on that date.

In view of the above quoted statements in the Commission's plan and order the court has felt justified and authorized in providing

for such purchase as not inconsistent with the plan. Disposition of the purchased bonds can later be determined by the reorganization committee and the court. They may be canceled or they may be utilized under the plan in acquisition of new securities which will become an asset of the reorganized company.

The court then took up the objections to the plan filed by most all interested parties, none of which were seriously pressed at the hearing (the Insurance Group Committee, typewritten record, p. 17; the Chase Bank, p. 22; the Untermyer Group—see objections; the Reconstruction Finance Corporation, pp. 17 and 18, and the Guaranty Trust Company, p. 19), counsel urging the approval of the plan in open court, reserving, however, the right to press their objections in detail if it was not approved by the court. The Central Hanover Bank and Trust Company, as Trustee under the first mortgage on the Rio Grande Junction Railway filed objections, mostly based upon the treatment the plan accorded the Junction bonds. These objections were eliminated, we assume, when the court granted their petition asking the Trustees be directed to purchase the Junction bonds 100% in cash, with interest.

The court has expressed its views on the various plans many times. (See Interim Memorandums August 30, 1940, December 6, 1940, March 6, 1941, August 14, 1943.)[1]

Furthermore, most of the objections made, and all those urged at the hearing, were passed upon by the Interstate Commerce Commission, whose decisions on the question involved this court must follow under the *Milwaukee* and *Western Pacific cases*, 318 U. S., so a brief reference to the plan now under consideration is all that seems necessary.

Three plans have been proposed by the Interstate Commerce Commission after hearings—all as required by §77. The first called "The Commission Plan," contained in its original report dated July 11, 1939 (233 I. C. C. 515); the second plan, set out in its report on further consideration, dated April 2, 1940 (239 I. C. C. 583); second supplemental report dated July 13, 1942 (254 I. C. C. 5); and the third supplemental report and order of June 14, 1943, certified to this court by the Commission on June 28, 1943 (254 I. C. C. 349). The last is called Approved Modified Plan on the Basis of Consolidation with the Denver and Salt Lake, with an Alternative Approved Modified Plan, without Consolidation with the Denver and Salt Lake.

The provision in former plans for an immediate loan of $2,250,000 is eliminated as unnecessary and on the basis of consolidation

[1] These four interim memorandums are not printed herein.

with the Denver and Salt Lake, the total capitalization proposed is $155,173,127, as compared with $154,521,612 previously. Annual charges are: Fixed interest $1,694,941, instead of $6,381,921.29 before this Trusteeship. Prior contingent interest $498,318, contingent interest $1,364,133, and total charges before dividends on the preferred stock $4,584,689. Other details are shown in Appendixes A and B, attached hereto.* The plan calls for $38,573,680 new first mortgage bonds, and new income bonds in the amount of $29,750,184.

The objections of Guy A. Thompson, Trustee in Bankruptcy of the Missouri Pacific Railroad Company and the debtor, the Denver and Rio Grande Western Railroad Company, may be considered together, in so far as they present any question that this court at this time can consider.

The Missouri Pacific Railroad is the owner of 150,000 shares, or one-half of the non-par common stock—the Western Pacific Railroad owning the other half—and $608,800 of the preferred stock, and $1,000,000 of refunding and improvement mortgage bonds of the debtor, the Denver and Rio Grande Railroad Company. Their chief objection is that the Interstate Commerce Commission in every plan certified to the court, finds no value or equity in the common and preferred stock of the company, and that the owners are not entitled to participate in the plan; that the plan does not preserve their interests as stockholders by providing for the issuance to stockholders of options or warrants to receive or subscribe for on fair and reasonable terms common and preferred stock in the newly-reorganized company; that the plan fails to give full and lawful effect to the value of the debtor properties and the earning power thereof past, present and prospective. Further objection is made to the alleged failure of the Commission to make a valuation of the properties of the debtor, and also that the findings of the Commission that there is no equity for the owners of the stock, is not substantiated by substantial evidence.

The same parties further alleged a large part of the traffic carried or which may be carried by the debtor railroad is and will be bridge traffic which neither originates on nor is destined for points on the Denver and Rio Grande Western Railroad Company; that a large part of it passes through the Pueblo Gateway, the volume of which is, and has been in a large measure due to the fact that the Missouri Pacific Railroad Company has been a part owner of the Rio Grande, and unless this ownership is carried forward

*Appendixes A and B are duplicates of appendixes A and B attached to Commission's third supplemental report, pages 182 and 183. They are not reprinted herein as attachments to the court's opinion.

into the new company, this long-existing channel of trade and commerce through the Pueblo Gateway over the Missouri Pacific and Rio Grande will be substantially impaired and the volume decreased, and the co-operation necessary to cause such a large volume of traffic to move thereover can be had only by ownership by the Missouri Pacific trustee of stock of the new company equal to that held by the Missouri Pacific in the old Denver and Rio Grande Western Railroad Company.

Further, that the debtor's property can not be properly operated unless the gateways of Denver and Pueblo are maintained with equal vigor; that neither the Denver nor Pueblo Gateway be impaired, and the maintenance of these two gateways be maintained. That to accomplish this, full co-operation on the part of the debtor and the Missouri Pacific Railroad is necessary but can not be brought about unless the present ownership of the Missouri Pacific Trustee in the Denver and Rio Grande Western Railroad Company is carried forward into the new company.

All of these objections, except the last in respect to the Pueblo Gateway, are fully answered and rejected in the *Western Pacific Reorganization case*, 318 U. S. 448 and the *Milwaukee Reorganization case*, 318 U. S. 532 *(supra)*. This court has found there is sufficient evidence to support the findings of the Commission, and that legal standards have been followed.

True there has been a tremendous increase in bridge traffic of the Rio Grande over a period of years. In 1920 the percentage of bridge traffic to total tonnage was 6.95%. This has steadily increased year by year until 1942, when the percentage of bridge traffic to total traffic amounted to 35.93%, out of a total tonnage of 5,496,833 tons, and for 1943 is estimated at 40% of 7,000,000 tons. Without this business this railroad could not begin to support a capital structure of any size.

For many years and until the construction of the Moffat Tunnel and the Denver and Salt Lake and the Denver and Salt Lake Western—the Cutoff—the main route of the Rio Grande was through Pueblo, where connection is made with the Missouri Pacific running to St. Louis and the East. A large volume of east and west bridge traffic has always been exchanged between the two roads at that point. I don't think it can be successfully challenged that the Missouri Pacific is equally, if not more dependent on the Rio Grande for eastbound business from the Pacific Coast delivered at Pueblo than the Rio Grande is for westbound business received from the Missouri Pacific. The Cutoff route, giving the Rio Grande a direct route from Denver to Salt Lake and the Pacific Coast—approximately 170 miles shorter than the route from Denver

through Pueblo—established another important gateway at Denver where connections are made, and a great deal of bridge traffic east and west exchanged with the Burlington, the Rock Island and the Union Pacific. This business the Rio Grande otherwise would not enjoy. It almost equals that passing through the Pueblo Gateway and does not divert any business from the Missouri Pacific at Pueblo. This short line between Denver and Salt Lake enables the Rio Grande to become a transcontinental line, competing on schedules equal to the Union Pacific on the north and the Santa Fe and Southern Pacific to the south.

The figures indicate that in 1942 the Rio Grande handled one-third less tonnage through Denver via the Moffat Tunnel Route than through Pueblo; that traffic via each route has increased in recent years. The proportion through each gateway has remained fairly constant since 1938 and while local traffic has declined in relative importance to bridge traffic, such traffic has not declined in actual tonnage. The fact is that both local and bridge traffic have shown an almost uninterrupted increase since the Trusteeship in 1935. In 1942 the Rio Grande handled 7,243,691 tons that originated on its lines, and 8,053,665 tons received from connecting carriers. In 1935 under Missouri Pacific control the property originated 4,404,574 tons of freight, and received 2,774,451 tons from other lines. The debtor's tonnage east and west through Pueblo increased 175% the total tonnage handled by the system increased 113% between 1935 and 1942 while freight originating on Class 1 railroads in the United States increased only 80% during the same period.

Passenger service from Pueblo to western and southwestern Colorado is now furnished by the Rio Grande Motor Way, and in many respects is far superior to railroad service due to more frequent as well as faster schedules. No freight train schedules through Pueblo have been canceled.

These figures indicate that under an impartial management, actuated by the best interests of the road and its customers, the Pueblo Gateway has not been hurt and demonstrates that under such a management the Missouri Pacific has exchanged more business with the Rio Grande at Pueblo during the Trusteeship than it did when it and the Western Pacific were in control. If necessary it can be shown that the Missouri Pacific control during past history of the property has been a detriment to the road and its security holders.

For these reasons the court fails to see the force of these arguments. Railroad traffic, like water, seeks its own level, and it is advantageous to both roads to exchange business at Pueblo and

maintain it as a gateway for transcontinental, or bridge traffic, irrespective of the control of one of the properties over the other.

The court is convinced from its experience with this property through two receiverships that it is for the best interests of this railroad and its security holders that it be maintained as an independent property free of control by any one road or financial group and free to make such deals with its connections as it deems fit. Reference is made to the provision of the plan under which all the voting stock of the new company both preferred and common is to be deposited in an escrow voting trust under a ten-year escrow agreement, under which either class of stock may be sold by the voting trustees subject to the approval of the Commission, and the consent of the holders of two-thirds of the escrow receipts representing the preferred and common, at a price advantageous to the interests of the new company. Under this provision control of the property can be purchased by the Missouri Pacific if it is for the best interests of the debtor.

The court has given a good deal of thought to this question during the Trusteeship, and is of the opinion that if the Missouri Pacific continues the service it maintains east from Pueblo and its splendid force of solicitors on the Coast, it will enjoy its fair proportion of the total bridge traffic moving east and west over the Rio Grande. It is not claimed, and can not be said that the Trustees have in any way favored Denver over the Pueblo Gateway. The Rio Grande is the middle link between its eastern connections both at Denver and Pueblo, and the Southern Pacific and Western Pacific at Salt Lake and Ogden, and has little opportunity to divert business from one gateway to the other.

Under the plan now before the court the Rio Grande Western first trust 4s get 73.5% of their claim in new first mortgage bonds and 26.5% in income bonds, as against 71% and 29%, respectively, under the plan rejected by the court while the Reconstruction Finance Corporation notes get 37.4% in first mortgage bonds and 62.6% in income bonds, and the Junction 5s having been purchased, the objections of the court to the former plan are in part at least corrected.

This property has gone through bankruptcy four times during its short history. These recurring financial crises in its affairs have been due in part to excessive capital structures and high fixed charges which the property has been wholly unable to earn under the management in control. In each reorganization the capital structure has not been cut to a level the earnings could support. Our experience with the property in two of these reorganizations convinces us that its financial troubles have been due in part

to absentee management wholly out of touch with the people and territory served. The court has suggested to the Commission more than once that the members of the reorganization committee and the directors of the new company should be residents of Colorado and Utah and their meetings should be held in Denver the main office of the debtor.

We have also suggested that the capital fund and depreciation fund be earmarked in cash and used only for those purposes. The Commission, however, has not accepted these views and while the court is still convinced they are for the best interests of the property and its security holders, this difference of opinion is not of sufficient importance to justify rejection of the plan.

It is suggested by competent railroad authorities that the only solution for the American railroads in the coming post-war competition is to build super-railroads to meet this competition. Great improvement in railroad plants and equipment will be required, together with many technical improvements—all at a very large cost. It involves intensive physical developments of roadbed and line, and motive power of such high capacity that maximum size freight and passenger trains can operate over long distances without intermediate speed restrictions due to adverse physical characteristics. The most modern standards of grade and curves and higher standards of design for all the components of the railroad plant must be adopted. Funds for this program must be obtained from earnings, depreciation reserves and new financing.

The court, being satisfied that the present plan complies with the provisions of subsection (b), (d), (e), of §205, Tit. 11, U. S. C. A., is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and conforms to the requirements of the law of the land regarding the participation of various classes of creditors and stockholders, and that all amounts to be paid by the debtor for expenses and fees incident to the reorganization have been fully disclosed, and provides for the payment of all costs of administration, and all allowances made or to be made by the judge, does hereby approve the plan in accordance with law.

Findings and an order in accordance herewith will be entered.

October 25, 1943.

(Printed) J. FOSTER SYMES,

District Judge.

United States District Court

FOR THE DISTRICT OF COLORADO

No. 8669

Filed Oct. 25, 1943.
G. WALTER BOWMAN,
Clerk.

In the Matter of

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, *Debtor.*

In Proceedings for the Reorganization of a Railroad.

ORDER NO. 495

ORDER APPROVING PLAN OF REORGANIZATION.

These proceedings coming on for hearing on the modified plan of reorganization for The Denver and Rio Grande Western Railroad Company (hereinafter called the Debtor) and The Denver and Salt Lake Western Railroad Company (hereinafter called the subsidiary debtor), approved by the Interstate Commerce Commission (hereinafter called the Commission) in its third supplemental report and order entered June 14, 1943 (hereinafter called the Plan and certified to this Court by the Commission on June 28, 1943, together with the transcript of all the proceedings before the Commission and a copy of its said third supplemental report and order approving the plan, and the Court having considered the entire record in these proceedings, including said transcript of all proceedings before the Commission and the evidence adduced and arguments presented at the hearing before this Court beginning on September 13, 1943.

THE COURT FINDS:

1. The findings and conclusions of the Commission stated in its Original Report of July 11, 1939 (Printed Record 5047–5200), its report on further consideration dated April 2, 1940 (P. R. 5815–5881), its second supplemental report dated July 13, 1942 (P. R. 9129–9258) and its said third supplemental report and order of June 14, 1943 (P. R. 10077–10181), as to each of said reports as modified by all subsequent said reports, are supported by evidence and are correct in fact and law and are adopted as findings and

conclusions of this Court, both as to liens of mortgages and otherwise without limitation, as fully as if set out at length herein.

2. The Plan:

(a) Includes provisions modifying and altering the rights of creditors of the Debtor and the subsidiary debtor;

(b) Provides for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that after due consideration of the probable prospective earnings of the property in light of its earnings experience and all other relevant facts, there will be adequate coverage of such fixed charges by the probable earnings available for the payment thereof;

(c) Provides adequate means for the execution of the plan; and

(d) In all other respects complies with the provisions of subsection (b) of Section 77 of the Bankruptcy Law, as amended.

3. The Plan:

(a) Is fair and equitable;

(b) Affords due recognition to the rights of each class of creditors and stockholders;

(c) Does not discriminate unfairly in favor of any class of of creditors or stockholders;

(d) Will conform to the requirements of the law of the land regarding the participating of the various classes of creditors and stockholders; and

(e) Provides for the payment of all costs of administration and all other allowances made or to be made by this Court.

4. (a) By Order No. 282 entered May 6, 1940 (P. R. 5930–5934) this Court required that each and every individual or corporation having or desiring to present any claim for expenses and fees incident to the reorganization herein should file such claim in the form of a petition in the office of the clerk of this Court on or before June 1, 1940 and that a copy of each such petition should be forwarded by the Clerk of this Court to the Commission for the fixing of a maximum limit with respect to the amounts to be allowed for

such expenses or fees. Petitions for such allowances were filed by numerous parties to this proceeding, such petitions generally covering the period prior to May 20, 1940, as suggested by the Bureau of Finance of the Commission in a notice sent to all parties in interest. By its Report and Order dated August 26, 1940 (P. R. 6786–6846) the Commission fixed the respective amounts stated therein as the maximum limits of final allowances to be paid out of the estate of the Debtor, as reasonable compensation for all services rendered and as reimbursement for all actual and reasonable expenses incurred by such petitioners and their counsel and technical advisers, in connection with the proceedings and plan of reorganization of the debtor to May 20, 1940, without prejudice to further allowances of fees and expenses for periods subsequent thereto upon appropriate supplemental petitions. By Order No. 333 entered April 14, 1941 (P. R. 7755) this Court made reasonable allowances within the maximum limits so fixed to certain of such petitioners, and denied allowances to others of said petitioners.

(b) By Order No. 463 entered July 1, 1943 (P. R. 10196) this Court required that each and every individual or corporation having or desiring to present any claim for compensation for services rendered or for expenses (including reasonable attorneys' fees) either under clause (12) of subsection (c) of Section 77, or otherwise, should file such claim in the form of a petition in the office of the Clerk of this Court on or before August 23, 1943, such petitions to cover all such services rendered and expenses incurred up to and including July 1, 1943; and said order further provided that a copy of each such petition should be transmitted by the Clerk of this Court to the Commission for the fixing of a maximum limit with respect to the amounts to be allowed for such compensation or expenses. Petitions for such allowances have been so filed by numerous parties to this proceeding, have been duly transmitted to the Commission, and are now pending before said Commission. No payments of compensation or expenses prayed for by said petitions shall be made by the Debtor or the subsidiary debtor or by any corporation or corporations acquiring the assets of the debtor or the subsidiary debtor, except in such amounts as may hereafter be approved as reasonable by order of this Court within such maximum limits as shall have been fixed by the Commission. No payment of expenses or fees incident to the reorganization for the period through July 1, 1943 shall be made by the debtor, the subsidiary debtor, or any corporation or corporations acquiring the assets of the debtor or the subsidiary debtor to any person except as prayed for in the petitions referred to in sub-paragraph (a) of this paragraph 4 or in this sub-paragraph (b) of this paragraph 4,

subject, as to the amounts prayed for in the petitions referred to in this sub-paragraph (b) to the maximum limits to be fixed by the Commission and the actual amounts to be fixed by further order of this Cou[illegible].

(c) Such additional amounts as may be required to be paid by the debtor, or the subsidiary debtor, or any corporation or corporations acquiring the assets of the debtor or the subsidiary debtor for services performed and expenses incurred (including reasonable attorneys' fees) after July 1, 1943, in connection with the proceeding and the Plan, and in connection with the carrying out of the Plan, if it be finally confirmed, can not be ascertained at this time, but such amounts will be subject to the approval of this Court within maximum limits hereafter to be fixed by the Commission.

(d) The approximate amounts to be paid by the Debtor, or the Subsidiary Debtor, or by any corporation or corporations acquiring the assets of the debtor or the subsidiary debtor, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of said hearing before this Court beginning on September 13, 1943, or at the date of this Order; so far as they can be so ascertained said expenses and fees are reasonable; and said expenses and fees as to those heretofore allowed are, and as to those hereafter allowed will be, within such maximum limits as are fixed by the Commission, and within the maximum limits so fixed have been or are to be subject to the approval of this Court.

5. By Order No. 95 entered November 23, 1936 (P. R. 2146–52) this Court divided the creditors and stockholders of the debtor and the subsidiary debtor into classes.

6. This Court has jurisdiction of the subject matter of these proceedings and of the debtor and the subsidiary debtor and their respective properties, creditors and stockholders, and all other parties having claims against or interest in the debtor or the subsidiary debtor or its or their property.

7. The foregoing findings shall be taken and deemed to be findings of fact, and in addition, to the extent appropriate, conclusions of law and also orders.

WHEREFORE, IT IS ORDERED:

FIRST: All objections heretofore filed herein to the Plan, and all claims heretofore filed herein for equitable treatment otherwise than through the Plan, are hereby severally overruled and denied

and the motions to remand the Plan to the Commission and to dismiss the proceedings are hereby severally overruled and denied.

SECOND: The Plan is hereby in all respects approved.

THIRD: The finding made by the Commission (P. R. 10143) that the interest of the holders of equipment obligations of the Debtor, equipment trust certificates of the Trustees and any other obligations under equipment leases or sales agreements will not be adversely and materially affected by the Plan is hereby affirmed.

FOURTH: The finding of the Commission (P. R. 5164 and 10175) that claims against the Debtors and their subsidiaries entitled to priority over their respective mortgages, claims for taxes levied, assessed or accrued against the Debtors, their subsidiaries or trustees, current liabilities and obligations incurred by the Trustees during the reorganization proceedings and claims arising from disaffirmance of executory leases or contracts of the Trustees pursuant to orders of the Court, in respect of which claims are filed or evidenced in accordance with orders of the Court, and the interests of parties to agreements and executory contracts with the Debtors assumed by the reorganized company, are not adversely and materially affected by the Plan is hereby affirmed.

FIFTH: The finding of the Commission (P. R. 10169) that the interests or equities of (1) all general unsecured creditors of the Debtor whose claims are not entitled to priority over the mortgages of the Debtor, (2) holders of preferred stock of the Debtor and (3) holders of common stock of the Debtor, have no value and nothing shall be distributable to them is hereby affirmed.

SIXTH: The Court reserves full jurisdiction to construe the Plan, to cure any defect, supply any omission and reconcile any inconsistency in the plan and to exercise all its powers under the Plan, all in such manner and to such extent as may be necessary or expedient to carry out the Plan effectively.

Dated October 25th, 1943.

(Printed) J. FOSTER SYMES,

U. S. District Judge.

A True Copy Teste

G. WALTER BOWMAN, *Clerk.*

By WILLIAM GRAF, *Deputy Clerk.*

[fol. 212]

MEMORANDUM ON CONFIRMATION OF PLAN—Filed November 1, 1944

By order of March 23, 1944 the Interstate Commerce Commission on April 26, 1944, submitted for acceptance or rejection by creditors of Classes 6, 7, 8, 10a, 10b and 11, 12a and 12b of the Denver & Rio Grande Western Railroad Company, the above debtor, and by creditors of Classes 1 and 2 of the Denver & Salt Lake Western Railroad Company, as therein provided, a plan for the reorganization of the debtor, the Denver & Rio Grande Western Railroad Company and of the Denver & Salt Lake [fol. 213] Western Railroad Company—a subsidiary-debtor—approved by the Commission in its Third Supplemental Report and Order of June 14, 1943 and approved by this court October 25, 1943.

Under date of July 4, 1944 the Commission has certified to this court the results of the vote on the submission of the plan of reorganization to the creditors of the Denver & Rio Grande Western Railroad Company, debtor, et al., as aforesaid, showing that said plan had been accepted by more than two-thirds in amount of the total of such claims voting, except that creditors of Class 11, holding $1,332,050 principal amount of Denver & Rio Grande Western Railroad Company General Mortgage Bonds, constituting 20.67% of the total amount of allowed claims of said class, voted for the plan, and creditors of said class holding $5,111,100 principal amount, or 79.33% of allowed claims of that class, voted to reject the plan.

Thereafter objections to the confirmation of the plan were filed by the debtor, the Denver & Rio Grande Western Railroad Company, by Guy A. Thompson, Trustee of the Missouri Pacific Railroad Company and by the City Bank Farmers Trust Company of New York, Trustee of the General Mortgage aforesaid. Said objections were set down for, and came on for hearing on August 30th and 31st, 1944, pursuant to notice to all parties. Full argument and hearing were had. Briefs were filed on behalf of said objectors, and in reply thereto by other trustees and interested parties.

[fol. 214] The claim of the General Mortgage Bonds on the effective date of the plan aggregated $43,500,000—

about one-fourth of the debtor's entire debt. It is claimed that when the capitalization of the new company was fixed at $155,173,127 on the basis of consolidation with the Denver & Salt Lake, and $143,528,027 for the debtor alone, if consolidation is not carried out, the Commission took care of every bond issue ahead of the General Mortgage (a junior issue), for 100% of their claims in new securities, and what was left over went to the General Mortgage. At that time the so-called Junction Bonds were in the hands of the public and in the plan the Commission provided that the Rio Grande Junction 5s—whose claim amounted to $2,758,333—should receive 77% thereof in First Mortgage Bonds, $2,123,916 par, and 23% in Income Bonds, or $634,417 par, and that after all the creditors ahead of the General Mortgage bondholders were taken care of, there was only enough common stock left over to give the General mortgages 10% of their claim in par value common stock.

That thereafter the wartime earnings of the property were so large that the cash jumped from $10,000,000 to $20,000,000, or better, and counsel says the court very appropriately in September, 1943, instructed the Trustees to buy the Junction Bonds at par and accrued interest and reduced the senior debt by that amount. That by reason thereof the trustee of the General Mortgage Bonds now asks; not for any change whatever in the valuation or [fol. 215] capitalization of the debtor, but simply an adjustment such as it says the Commission authorized to be made within the framework of the plan by a redistribution of the new securities that the plan allots to the Junction Bonds, and in so doing maintain the same priority as before between the various issues. That it is simply a matter of accounting.

It is argued that in several other railroad reorganizations, that between the time the Commission put down a plan and the time it got to the court for action, the surplus cash of the respective debtors increased very much so the senior debts could be reduced. That in cases that have come down from the Interstate Commerce Commission since last September it has been said if the surplus cash is used to reduce the senior debt and stops there, for practicable purposes the capitalization of the new company is reduced below that authorized and what the Commission has found the debtor should and can reasonably

support. That the way to adjust is to take the new securities allotted to the senior bonds or debt thus paid off and redistribute them, keeping everybody's position relatively the same. That this would shove everybody up a little and give the junior issues better treatment.

It is further urged by this mortgage trustee that the reorganization committee or court should make this adjustment on the basis of the distribution the Commission has followed, and distribute the $2,758,333 bonds set aside to exchange for the Junction Bonds in the plan, keeping the same priorities.

[fol. 216] In support of this theory attention is directed to the New Haven reorganization, 54 Fed. Supp. 595 and 631. In that case there were certain first and refunding mortgage bonds up as collateral to secure six bank loans aggregating $26,000,000.

The court took $18,000,000 of surplus cash resulting from wartime earnings and with the Commission, decided they could apply it to reduce the claims of the banks by paying the accumulated interest thereon. The problem then was to make a redistribution of the $18,250,000 in bonds provided for in the plan for that purpose, and the court held it should be redistributed along the line that counsel are contending should be done here.

Judge Hincks says by paying off the accumulated interest thereon the secured claims were reduced, so that only $84,800,000 in fixed interest bonds were required, this resulting in a capital structure with a bonded indebtedness less than that which the Commission had found the railroad could reasonably support. Thus a block of $6,000,000 in fixed interest bonds and $11,680,000 in income bonds became available to sweeten the treatment previously proposed for all mortgage creditors. And this was done. Judge Hincks, however, adds that all creditors agreed that these excess securities should be distributed to all secured creditors not already awarded the full value of their claims in fixed interest bonds.

Judge Hincks then went further and paid the bank loans in full out of surplus cash and said, I quote (p. 608):

[fol. 217] "I doubt whether these conclusions require that the plan be returned to the Commission. I incline to believe that the necessary correction can be accomplished within the framework of the plan in

complete conformity with all the valid findings of the Commission."

By analogy counsel argue that in the Rio Grande situation the $2,123,916 Fixed Interest Bonds and $634,417 of Income Bonds allocated to the Junctions should be used to sweeten the treatment previously proposed for all mortgage creditors who have not already been awarded the full value of their claims in Fixed Interest Bonds.

What Judge Hincks did was to pay the bank loans off in full out of surplus cash, stating he believed this action could be accomplished by the court within the framework of the plan without returning it to the Commission, and that this action was based upon the findings of the Commission and was consistent with its limitations and within the power of the judge to make. Later the Commission filed a report approving everything Judge Hincks had done in this respect.

Judge Hincks, however, after expressing doubts whether his action required the plan be returned to the Commission stated, p. 608:

> "I incline to believe that the necessary correction can be accomplished within the framework of the plan in complete conformity with the valid findings of the Commission."

[fol. 218] In view of the sharp division between the functions of the district courts and the Commission in § 77 reorganizations announced by the Supreme Court (Ecker v. Western Pacific R. Corp., 318 U. S. 448 and Group of Investors v. Milwaukee R. Co., 318 U. S. 523), the action of Judge Hincks is hardly authority—at least until approved by an appellate court. What he really did was to make his ruling and then ask the Commission to approve.

In the final analysis, however, what Judge Hincks really did in the New Haven case was to pay off an obligation of the estate, while here the court in its treatment of the Junction Bonds did not pay off a debt, but only purchased securities, thereby giving the debtor control of another railroad property, to wit, the Rio Grande Junction Railroad Company—a necessary part of its system.

The plan itself does not contemplate the capitalization of the new company be absolutely static, but subject to

change, because it provides, as Mr. Gibson well points out (p. 10142 of the printed court record and P. 66 of the court reprint):

> "The capitalization of the new company, as of January 1, 1943, after consummation of the plan, including the merger or consolidation of the Salt Lake, shall consist substantially of the following securities, excluding those to be pledged, the amounts stated being subject to reduction to the extent, if any, that matured interest proposed to be funded in the plan is [fol. 219] paid, and as equipment obligations or other liabilities are paid or reduced, * * *."

Frankly, I do not believe the court has the power to make the reallocation requested by the General Mortgage trustee, because it would, in effect, change the allotment of every security dealt with in the plan.

Counsel argue that the court has the power asserted under 5, T, p. 105 of the printed plan, where the Commission says:

> "The court may cure any defect, supply any omission, or reconcile any inconsistency, in such manner or to such extent as may be necessary or expedient to carry out the plan effectively."

The Commission, however, has no power to delegate powers or duties to the court. It is not claimed there is a defect in the plan, nor that there is any omission or inconsistency.

The modification in the Milwaukee case referred to is contained in "Summary of Second Supplemental Report of the Commission" dated December 6, 1943, and says:

> "This report approves certain adjustments of the plan of reorganization of the Chicago, Milwaukee, St. Paul & Pacific Railroad Company approved * * * June 4, 1940."

Furthermore it appears in said report that the Commission itself distributed $52,038,0[illegible] of cash on account of interest accruing during the trusteeship, not authorized [fol. 220] by the court. Next the Commission stated that in view of the payment of a bank loan and the reduction in amount of the claim of the Reconstruction Finance Corporation since the date of the plan, and the distribution

to creditors of $5,000,000 of first mortgage bonds previously set aside for new money, approximately $7,096,336 of first mortgage bonds will be issued to the Milwaukee & Northern first mortgage bondholders, Milwaukee & Northern consolidated mortgage bondholders and the debtor's general mortgage bondholders.

> "in addition to the amounts of such bonds allotted to them in the plan previously approved."

In other words the Commission itself made an allocation, which in the case at bar it is urged the court make.

Next the objectors in support of their objections complain of a too low capitalization of the new company. In view of the past history of this property it is hard for this court to take stock in any such argument. The court has attempted to dispose of it in previous opinions, and it has been rejected by the Supreme Court (infra). The permissible capitalization is a matter entirely under the jurisdiction of the Interstate Commerce Commission. Ecker v. Western Pacific R. Corp. (supra), p. 483.

In the Milwaukee case (supra), the Supreme Court said, p. 541:

> "Certainly there is no constitutional reason why earning power may not be utilized as the criterion for [fol. 221] determining value for reorganization purposes. And it is our view that Congress when it passed §77 made earning power the primary criterion."

A factor that cannot be overlooked in capitalizing earnings is the steady and material reduction in average revenue per ton mile—the basic index of the gross yield from transportation service. The average revenue of this road per ton mile declined from 1.765 cents in 1921 (Rio Grande annual report 1936, p. 27), to 0.994 cents in 1943 (annual report 1943, p. 29), a decrease of almost 50%.

Other factors which dampen optimism as to the continuation of higher earnings in the future are income taxes which this road has not been liable for since 1939, except 1942 and 1943, and very large increases in operating expenses, as shown in the Commission's 1939 report on a plan. This shows greatly increased operating costs, such as wages, fuel, materials and supplies of all kinds, and more than

offsets the economies effected by the Improvement Program. Dividends have not been paid on either class of Rio Grande stocks since 1911.

A study of the traffic gains of the railroads of the country indicates that in the third year of complete wartime prosperity the western carriers will be the most outstanding beneficiaries of the increase in railroad gross earnings. For many years before the war the western carriers suffered sharply reduced revenues, wholly inadequate to cover [fol. 222] bond interest and fixed charges. Most of the bankrupt railroads are located west of the Mississippi River.

In the early upswing of business in 1940 and 1941 the western group failed to match the operating improvement made by the eastern carriers, and it was not until 1942 that an abrupt change in operating conditions resulted in the western roads reaping the harvest of profits comparable to the gains of the eastern roads.

The reasons for this are the tremendous increase in transcontinental traffic due to the war in the Pacific, restrictions on shipping, and the closing of the Panama Canal. Also the lessening of truck competition, which in the past played havoc with the western carriers, but has largely ceased as a competitive factor since 1942. Also passenger business has returned to the railroads in large volume due to these wartime limitations on motor transportation. The Southern Pacific, for instance, shows an increase in passenger revenues from $24,000,000 in 1940 to $124,000,000 in 1943 and may reach $150,000,000 in 1944. The St. Louis & San Francisco shows an increase in passenger revenue from $3,000,000 in 1940 to $23,000,000 last year. The expected shift in war equipment to the Pacific combat area may sustain these increased earnings of western railroads for a few years after the war.

Another favorable factor is: Normally eastbound railroad traffic of the western and eastern carriers is heavier. War traffic demands have, however, brought about a diver- [fol. 223] gent shift for the two groups, and there are indications that this factor will last as long as the war with Japan. But the end to the war will undoubtedly result not only in a sharp contraction of freight tonnage but also restore the former unfavorable balance of train movements.

It is estimated that 60% of the inflated earnings of the debtor for the last three or four years is due to Government and war business both freight and passenger, but as has already been pointed out by this court, as well as the Supreme Court, war earnings are not a sufficiently stable basis for new capitalization.

Counsel refers to new industries located along the line of this debtor, but does not list them or state whether they are permanent or not. Of the few plants located along the line known as war industries, Camp Hale—a training camp at Leadville, Colorado—has been abandoned and practically no personnel left. The Kalunite plant, located in the Roper Yards outside of Salt Lake—which treats alunite ores—is still operating, but it is anticipated it will not survive the war. The Remington Arms plant at Salt Lake has been closed and is now used only as a storage depot. The activities of the Remington plant at Denver are greatly curtailed. The Kearns Replacement Center in Utah, while still fairly active will eventually be closed. Camp Carson at Colorado Springs is already greatly reduced in size. The Naval Supply Depot at Clearfield, Utah, and the Columbia Steel plant at Geneva, Utah, are [fol. 224] the only ones promising any permanency as business producers of this property.

The plan gives the old Junction Bonds $2,123,916 in the new First Mortgage Bonds and $634,417 in new Income Bonds. Under the priority rule of the Boyd case, 228 U. S. 482, in any reallotment of these senior securities they would mostly go to the First Trust 4s and the Western Consolidateds, and the so-called sweetening process would increase the General Mortgage Bonds' allotment very little, if any. The most they would get would be more common stock which has little or no value, and would only dilute the value of the common stock they now get. True they might get more stock—that is more pieces of paper—the total value of which would be little, if any more, than of that they now get.

It is said the debtor's income available for interest during trusteeship aggregated $28,700,000, which according to counsel, was used by the Trustees to carry out an improvement program, and that this expenditure is reflected in greatly increased earnings that would well support an increased capitalization.

The net operating income of this property available for interest, as restated under the plan, for the year 1941 was $3,428,000; 1940, $1,966,878; 1939, $1,235,209, and in 1938 and 1937 there was a deficit. The net after interest accruals and other charges under the new plan for 1941 was $683,082. In 1939 there was a deficit for said purpose of $502,808, and for 1938 there was a deficit of $2,172,128; in 1937 a deficit of $3,840,548.

[fol. 225] From the calendar year 1932, up to and including the calendar year 1940, there was only one year, 1933, when there was available for interest on the new Income Bonds the amount the plan calls for, and then only by disregarding the cumulative interest provision of the plan. This was at a time when every economy was practiced by the debtor at the expense of maintenance of the property. In addition this was one of the years in which money was borrowed to pay current taxes and interest not earned on the Denver & Rio Grande First Consolidated and the Rio Grande Western First Trusts.

The court in its plan of March 6, 1941 gave the General Mortgage bondholders more common stock than does the approved plan. The Commission, however, could not agree with our views, and it would seem to be a useless gesture for the court to make the same error again assuming we had the power.

A basic requirement of any reorganization, according to the Supreme Court

> "is the determination of a capitalization which makes it possible not only to respect the priorities of the various classes of claimants but also to give the new company a reasonable prospect for survival. * * * Only 'meticulous regard for earning capacity' * * * can afford the old security holders protection against a dilution of their priorities and can give the new company some safeguards against *the scourge of overcapitalization.*" (Emphasis ours.) Group of Investors v. Milwaukee R. Co. (supra), pp. 540-41.

[fol. 226] Boiling the argument down, in the final analysis it is the old one of security holders having made an unwise investment and now look to the bankruptcy court to restore values by some sleight of hand or legerdemain, which never existed or have been wiped out by mismanagement. A § 77 bankruptcy reorganization proceeding,

however, contemplates the scaling down of all claims and that the security holders may take a substantial loss. The procedure is not one designed to recoup losses.

The $25,000,000 or more the Trustees have expended in the Improvement Program inures to the benefit of the common stock. If the latter is worth anything it is as much due to these expenditures as to any other factor. This, with the increase in current assets and wartime earnings which counsel seem to believe are permanent, constitute the only equity behind the preferred and common stock.

No security holder is getting what he thinks he should. All have suffered losses. The plan is not the best imaginable—it is the only one of several that have come before the court with the practically unanimous approval of all interested parties. And in the court's opinion, any further delay or resubmission to the Commission would prejudice the successful and speedy consummation of the reorganization of this debtor and its removal from the court—a consummation devoutly desired.

For the reasons stated the court does not believe the objections under consideration are tenable, and the plan [fol. 227] having been accepted by two-thirds in amount of the total voting of the allowed claims of each class voting except the one, such acceptances not having been made or procured by any means forbidden by law the court, after full hearing, hereby finds it makes adequate provision for fair and equitable treatment for the one class of creditors rejecting it, to wit, the holders of the General Mortgage Bonds, and their rejection is not reasonably justified in the light of the respective rights, and all of the relevant facts and interests of those rejecting it. And furthermore, that it conforms with all provisions of subsection (e) of § 205, Tit. 11, U. S. C. A.

A recapitulation of the vote on the plan indicates that 40.77% of the total outstanding claims in the hands of the public voted to accept the plan, only 4.99% voted against. It would seem inequitable to reject this plan, approved, as it is, by all except a small minority of the total securities voting, especially if we consider the length of time the property has been in the hands of the court, and the exhaustive hearings on these same objections that have been had both before the Interstate Commerce Commission and this court.

But even if the petition of the City Bank were granted the so-called Insurance Group which approves this plan would, in any reallocation, receive the senior securities that the objecting trustee refers to. This because Mr. Justice Douglas in the Milwaukee opinion (supra), states that compensation must be given to the senior creditors for [fol. 228] their sacrifice of their senior position in taking junior securities, and it is only after their claim is fully satisfied that anything can be allocated to junior liens.

The General Mortgage bondholders say, in effect, that the $2,700,000 in new First Mortgage and Income Bonds thus released would go to the senior creditors; that this in turn would free an equal amount of junior securities now allotted to senior bondholders, which would, in turn, go to the second lienors, thus freeing finally the most junior securities, that is stock, to the General Mortgage Bonds. In the opinion of the court such a reallocation of securities can only be made by the Commission. The net result would be that the senior creditors would receive a larger amount of senior securities than they do now.

The only class of creditors who have failed to assent are the most junior in this picture who, as a condition of their assent, ask for an increase in the total capitalization. But, for reasons stated and authorities cited, this is a matter clearly within the power of the Commission, which has rejected the argument more than once.

As to the non-assenting classes the language of the statute is:

> "if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, [fol. 229] that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it."

And:

> "that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts."

And finally:

> "that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e)."

I am satisfied, and find after hearing, that all the requirements of the statute have been met; that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it, and it is hereby confirmed.

Proper findings and order as required may be prepared and submitted by counsel.

J. Foster Symes, District Judge.

November 1, 1944.

[File endorsement omitted.]

[fol. 230] In United States District Court

Ordering Confirming Plan of Reorganization—Filed November 29, 1944

These proceedings having come on to be heard on August 30-31, 1944, pursuant to the order of this Court entered July 20, 1944, for a consideration of the confirmation of the Modified Plan of Reorganization (hereinafter called the Plan) for The Denver and Rio Grande Western Railroad Company (hereinafter called the Debtor) and The Denver and Salt Lake Western Railroad Company (hereinafter called the Subsidiary Debtor) approved by the Interstate Commerce Commission (hereinafter called the Commission) in its Third Supplemental Report and Order entered June 14, 1943, and approved by Order of this Court entered October 25, 1943, and there being filed with the Court a certificate of the Commission dated July 4, 1944, and other data with respect to the submission of the Plan to creditors for acceptance or rejection, and evidence having been received and the Court having considered the entire record in these proceedings, including the transcript of all proceedings before the Commission, the transcript of all prior proceedings before the Court and the evidence [fol. 231] adduced and arguments presented at the hearing before the Court beginning on August 30, 1944, and being fully advised in the premises,

The Court Is Satisfied and Finds that:

1. This Court has jurisdiction of the subject matter of these proceedings and of all the parties hereto and has

jurisdiction over the Debtor and the Subsidiary Debtor and their respective properties, wherever located, and of their respective creditors and stockholders and all other persons having claims against or interests in the Debtor or the Subsidiary Debtor or its or their property.

2. This Court has heretofore approved the Plan, a copy of which is on file herein and by reference made a part hereof. On October 25, 1943, this Court filed an opinion stating its conclusions and reasons for such approval and entered an order containing the findings of this Court and approving the Plan (Order No. 495), and certified copies of said opinion and order were sent to the Commission.

3. Pursuant to an Order entered by this Court on July 17, 1936 (Order No. 69, Rec. 1575) and an Order entered by this Court on September 4, 1935 (Order No. 81, Rec. 1818), lists of all known bondholders, creditors and stockholders of the Debtor and the Subsidiary Debtor, together with other information in connection therewith in satisfaction of all requirements of Section 77 of "An Act to Establish a Uniform System of Bankruptcy Throughout the United States" as amended (hereinafter called Section 77), were prepared and filed with the Clerk of this Court on September 9, 1936 (Rec. 1929) and September 15, 1936 (Rec. 1986) and copies thereof were duly transmitted to the Commission. By request of the Commission in July, 1943, the Trustees made a comprehen- [fol. 232] sive search by examination of records, circular letters of inquiry and advertisements in various newspapers, commercial and financial journals and investment services to modernize and perfect the original lists so filed and the new lists so prepared were duly transmitted to the Commission on or about April 19, 1944, and supplemental lists were so transmitted on or about April 25, 1944.

4. On or about April 26, 1944, the Commission, in conformity with subsection (e) of Section 77 and pursuant to its said Order dated March 23, 1944, duly submitted the Plan for acceptance or rejection to the creditors of the Debtor of Classes 6, 7, 8, 10, 11 and 12 as classified by an Order entered by this Court on November 23, 1936 (Order No. 96, Rec. 2146) and to the stockholders and creditors of the Subsidiary Debtor of Classes 1 and 2 as classified

by an order entered by this Court on February 5, 1937 (Order No. 110, Rec. 2483).

5. By said Order No. 495 entered October 25, 1943, this Court affirmed the finding of the Commission that the interests or equities of (1) all general unsecured creditors of the Debtor whose claims are not entitled to priority over the mortgages of the Debtor, (2) holders of Preferred Stock of the Debtor and (3) holders of Common Stock of the Debtor, have no value. Creditors of Classes 3, 4 and 5, as classified by said Order dated November 23, 1936, and holders of claims referred to in paragraphs Third and Fourth of said Order of October 25, 1943, are not materially and adversely affected by the Plan.

6. By an Order entered September 16, 1943, this Court directed the Trustees to purchase the Junction Bonds at a price specified therein; substantially all of such bonds have been so purchased; and the Trustees, subject to further order of this Court, are hereby directed to hold the aggregate purchase price for such of said bonds as have not here-
[fol. 233] tofore been purchased in a separate account for the purpose of purchasing such bonds.

7. In view of the provisions of the Plan, the findings of the Commission contained in its Order of June 14, 1943, the findings of this Court contained in said Order of October 25, 1943, and the matters referred to in paragraph 6 hereof, submission of the Plan to any class or classes of creditors or stockholders other than those to which it was submitted as aforesaid was not required under subsection (e) of Section 77. The United States is not a creditor of the Debtor or of the Subsidiary Debtor on claims for taxes or customs duties, unless it be on claims for the payment of which the Plan duly provides and the Plan need not be submitted to the United States of America, the President of the United States, or any officer or agency designated by him.

8. The Commission by its certificate dated July 4, 1944, duly filed herein has duly certified to this Court the fact, form, method and results of such submission of the Plan for acceptance or rejection. Copies of the Commission's said Order of March 23, 1944, of the Commission's said certificate of July 4, 1944, and of the lists of creditors to whom submission was made and duplicate originals of the

ballots returned to the Commission were duly filed in this proceeding.

9. Thereafter said Order of this Court was entered on July 20, 1944, setting a hearing for the consideration of the confirmation of the Plan. Notice of such hearing was given in accordance with the provisions of said Order. The notice so given constitutes due notice to the Debtor, its Trustees, the Subsidiary Debtor, its Trustees, the stockholders and creditors of the Debtor and of the Subsidiary Debtor, the Commission, the Secretary of the Treasury of the United States and all other interested parties.

[fol. 233a] 10. The Plan has been duly submitted to all classes of security holders entitled to vote thereon and the form and method of such submission fully satisfy all requirements of law.

11. The Plan has been duly accepted by or on behalf of creditors and stockholders of each class to which submission is required under subsection (e) of Section 77 holding more than two-thirds in amount of the total of the allowed claims of each class, which have been reported in said submission and in said certificate of the Commission as voting on the Plan except the holders of the General Mortgage Bonds of the Debtor.

12. Such acceptances have not been made or procured by any means forbidden by law.

13. The Plan makes adequate provision for fair and equitable treatment for the interests or claims of the holders of the General Mortgage Bonds of the Debtor.

14. The rejection of the Plan by the holders of the General Mortgage Bonds of the Debtor is not reasonably justified in the light of their respective rights and interests and all the relevant facts.

15. The Plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of subsection (e) of Section 77, and, without limiting the generality of the foregoing language,

> (i) The plan complies with the provisions of subsection (b) of Section 77, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in

favor of any class of creditors or stockholders, and conforms and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders;

(ii) All amounts to be paid by the Debtor or the Subsidiary Debtor, or by any corporation or corpora-
[fol. 234] tions acquiring the assets of the Debtor or the Subsidiary Debtor, for expenses and fees incident to the reorganization, have been fully disclosed so far as they could be ascertained at the date of such hearing, namely, for the period through July 1, 1943; the Commission has fixed maximum limits in respect to the amounts to be allowed for such expenses and fees and by an order entered April 14, 1941 (Order No. 333, Rec. 7755) and by an order entered May 3, 1944 (Order No. 536); this Court made such allowances as it deemed reasonable within such maximum limits. Such additional amounts as may be required to be paid by the Debtor or the Subsidiary Debtor, or any corporation or corporations acquiring the assets of the Debtor or the Subsidiary Debtor for expenses and fees incident to the reorganization in respect of the period after July 1, 1943, can not be ascertained at this time, but, by virtue of the Plan and this Order, such amounts will be subject to maximum limits therefor to be hereafter fixed by the Commission and will within such maximum limits be subject to the approval of this Court; and

(iii) The Plan provides for the payment of all costs of administration and all other allowances made or to be made by this Court.

16. By various orders entered in this proceeding the Trustees, or the Debtor, while under the control of this Court, have been authorized to enter into various agreements, contracts, instruments and leases extending beyond the period of this reorganization proceeding. Said orders provide that as a condition to the conclusion of these proceedings or the turn-over of the estate the Debtor or any person or corporation acquiring the Debtor's property shall be or become bound by all the terms and provisions of such agreements, contracts, instruments and leases. [fol. 235] The Plan and this Order provide for the adoption

of all such agreements, contracts, instruments and leases by the New Company, and such conditions are accordingly satisfied.

17. The Plan duly satisfies all of the requirements of Section 77 for approval by the Commission and this Court and for confirmation by this Court and all steps necessary to be taken in connection therewith, and all things necessary to be done in connection therewith, by the Commission, this Court, the Debtor, its Trustees, the Subsidiary Debtor, its Trustee and all other persons, have been taken and performed in the manner and within the times required in Section 77 and in conformity with all requirements of Section 77 and all other applicable law.

18. The Plan should now be confirmed.

19. The Court has on November 1, 1944, filed in this proceeding an opinion containing a statement of its conclusions and reasons for confirming the Plan.

20. In conformity with Section Q of the Plan, Insurance Group Committee has duly designated Richard K. Paynter, Jr., and Eugene A. Schmidt, Jr., to be members of the Reorganization Committee provided for in the Plan; The Chase National Bank of the City of New York, as Trustee, and City Bank Farmers Trust Company, as Trustee, have duly designated J. F. Fitzpatrick to be a member of the Reorganization Committee; and Reconstruction Finance Corporation has duly designated Frank C. Wright to be a member of the Reorganization Committee. Under said Section Q this Court is empowered to designate a member of the Reorganization Committee and upon such designation the Reorganization Committee will be duly constituted and will have the powers and authority provided for in the Plan as the Reorganization Committee and as the Voting Trustees provided for in the Plan.

[fol. 236] 21. The term "parties in interest", wherever used herein, shall, without hereby limiting the generality thereof, include the Debtor, the Subsidiary Debtor, all creditors and stockholders of the Debtor or the Subsidiary Debtor, all indenture trustees, all parties to these proceedings and all other parties in interest.

22. The findings herein shall be taken and deemed to be findings of fact, and, in addition, to the extent appropriate, conclusions of law and also orders.

It Is, Therefore, Ordered, Adjudged And Decreed That

(a) The Plan be, and it hereby is, confirmed, and all objections thereto are severally overruled.

(b) The provisions of the Plan and of this Order shall forthwith become and be, and are hereby declared to be, final and binding, upon the Debtor and the Subsidiary Debtor, and all of their respective stockholders, including those who have not, as well as those who have, accepted the Plan, and all creditors of the Debtor or the Subsidiary Debtor, secured or unsecured, whether or not adversely affected by the Plan, and whether or not their claims have been filed, and, if filed, whether or not approved, including creditors who have not, as well as those who have, accepted the Plan, and upon any and all other parties in interest.

(c) No payments shall be made by the Debtor or the Subsidiary Debtor or any corporation or corporations acquiring the assets of the Debtor or the Subsidiary Debtor for services performed or expenses incurred (including reasonable attorney's fees) after July 1, 1943, in connection with the proceeding or the Plan, or in connection with the carrying out of the Plan, or incident to the reorganization, except as may be hereafter authorized by further order of this Court within maximum limits hereafter to be fixed by the Commission.

[fol. 237] (d) The rights of all stockholders and creditors of the Debtor and the Subsidiary Debtor and of all other parties in interest shall be only those provided by the Plan.

(e) The Debtor, the Subsidiary Debtor and any new corporation organized to receive the properties of the Debtor or the Subsidiary Debtor upon the consummation of the Plan be, and each of them hereby is, authorized and directed, and shall have full power and authority, to take all steps, and do all things, necessary on its or their part to put into effect and carry out the Plan and the orders of this Court relative thereto, under and subject to the supervision and control of this Court, the laws of any State or the decision or order of any State authority to the contrary notwithstanding.

(f) The Court hereby designates John Evans to be a member of the Reorganization Committee.

(g) The Reorganization Committee, pursuant to the provisions of Section 77 and the Plan, and with all the powers and immunities provided in Section 77 or the Plan, shall have full power and authority, subject to the supervision and control of this Court, to put into effect and carry out the Plan and the orders of this Court relative thereto; provided, however, that the Plan shall not be submitted to the holders of the Income Bonds of The Denver and Salt Lake Railway Company, and the Plan shall not be consummated, until the appeal taken from this Court's said Order of October 25, 1943, shall be dismissed or finally decided in such manner as to affirm such Order and until any appeal taken from this Order shall be dismissed or finally decided so as to affirm this Order, or until further order of this Court.

(h) As provided in said Section Q of the Plan the members of the Reorganization Committee, in their capacity as members of such committee and in their capacity as Voting [fol. 238] Trustees shall not be liable for any action taken by them in good faith or by any person employed by them in good faith, except for their respective individual malfeasance or willful neglect. The members of the Reorganization Committee, and their successors, if any, and each of them, be, and they are and he is hereby, relieved of all personal liability to any person, firm or corporation for acts done pursuant to prior approval of this Court. The Reorganization Committee shall report to the Court all action taken by them without prior approval of this Court, and, upon approval by this Court, such members and each of them shall be relieved from all personal liability to any person, firm or corporation therefor. To the extent necessary to give effect to the provisions of this paragraph, the members of the Reorganization Committee shall be indemnified and held harmless against any loss, liability or expense by the Trustees, the Debtor, the Subsidiary Debtor and any corporation receiving the properties of any of them upon the consummation of the Plan.

(i) This order shall become, and it is hereby declared to be, effective immediately upon its entry in this proceeding by the signature of the Judge of this Court.

(j) The Court reserves full jurisdiction to construe the Plan, to cure any defect, supply any omission and reconcile any inconsistency in the Plan and to exercise all its powers under the Plan, all in such manner and to such extent as may be necessary or expedient to carry out the Plan effectively.

(k) The Court retains full jurisdiction of this proceeding and of all parties in interest for the purpose of entering such other and further orders as may be appropriate.

Dated November 29th, 1944.

By the Court, (S.) *J.* Foster Symes, *Judge.*

[File endorsement omitted.]

[fol. 239] United States Circuit Court of Appeals,
Tenth Circuit, November Term, 1944

Nos. 2906, 2907, 3106, 3107 and 3108

In the Matter of The Denver and Rio Grande Western Railroad Company, a Corporation, Debtor

No. 2906

The Denver and Rio Grande Western Railroad Company, a Corporation, Debtor, Appellant,

vs.

Insurance Group Committee; Reconstruction Finance Corporation; Wilson McCarthy and *Henry Swan*, as Trustees of The Denver and Rio Grande Western Railroad Company, a Corporation; the Chase National Bank of the City of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; City Bank Farmers Trust Company, a Corporation, as Trustee; The United States Trust Company of New York, as Trustee; and Central Hanover Bank and Trust Company, as Trustee, Appellees

Appeals from the United States District Court for the District of Colorado

[fol. 240] No. 2907

The Denver & Salt Lake Western Railroad Company, a Corporation, Debtor, Appellant,

vs.

Insurance Group Committee; Reconstruction Finance Corporation; H. Allyn Hicks, Jr., as Trustee of The Denver & Salt Lake Western Railroad Company, a Corporation; The Chase National Bank of the City of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; City Bank Farmers Trust Company, a Corporation, as Trustee; The United States Trust Company of New York, as Trustee; and Central Hanover Bank and Trust Company, as Trustee, Appellees

Appeals from the United States District Court for the District of Colorado

No. 3106

CITY BANK FARMERS TRUST COMPANY, a Corporation, as Trustee under the General Mortgage, February 1, 1924, of The Denver and Rio Grande Western Railroad Company, Appellant,

vs.

INSURANCE GROUP COMMITTEE; RECONSTRUCTION FINANCE CORPORATION; Wilson McCarthy and Henry Swan, as Trustees of The Denver and Rio Grande Western Railroad Company, a Corporation; H. Allyn Hicks, Jr., as Trustee of The Denver & Salt Lake Western Railroad Company, a corporation; The Moffat Tunnel Improvement District; Moffat Tunnel Commission; Guy A. Thompson, as Trustee of the Missouri Pacific Railroad Company; The Denver and Rio Grande Western Railroad Company, [fol. 241] a Corporation, Debtor; The Denver & Salt Lake Western Railroad Company, a Corporation; Subsidiary Debtor; State of Colorado; Colorado Public Utilities Commission; The United States Trust Company of New York, as Trustee; The Chase National Bank of the City of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; Central Hanover Bank and Trust Company, as Trustee; Untermyer Family Group; General Securities Company; and Bankers Trust Company, as Trustee, Appellees

Appeals from the United States District Court for the District of Colorado

No. 3107

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, a Corporation, Debtor; and The Denver & Salt Lake Western Railroad Company, a Corporation, Subsidiary Debtor, Appellants,

vs.

INSURANCE GROUP COMMITTEE; CITY BANK FARMERS TRUST COMPANY, a Corporation, as Trustee; Reconstruction Finance Corporation; Wilson McCarthy and Henry Swan,

as Trustees of The Denver and Rio Grande Western Railroad Company, a Corporation; H. Allyn Hicks, Jr., as Trustee of The Denver & Salt Lake Western Railroad Company, a Corporation; The Moffat Tunnel Improvement District; Moffat Tunnel Commission; Guy A. Thompson, as Trustee of the Missouri Pacific Railroad Company; State of Colorado; Colorado Public Utilities Commission; The United States Trust Company of New York, as Trustee; The Chase National Bank of the City [fol. 242] of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; Central Hanover Bank and Trust Company, as Trustee; Untermyer Family Group; General Securities Company; and Bankers Trust Company, as Trustee, Appellees.

Appeals from the United States District Court for the District of Colorado

No. 3108

GUY A. THOMPSON, as Trustee of the Missouri Pacific Railroad Company, Appellant,

vs.

INSURANCE GROUP COMMITTEE; CITY BANK FARMERS TRUST COMPANY, a Corporation, as Trustee; Reconstruction Finance Corporation; Wilson McCarthy and Henry Swan, as Trustee of The Denver and Rio Grande Western Railroad Company, a Corporation; H. Allyn Hicks, Jr., as Trustee of The Denver & Salt Lake Western Railroad Company, a Corporation; The Moffat Tunnel Improvement District; Moffat Tunnel Commission; The Denver and Rio Grande Western Railroad Company, Debtor; The Denver & Salt Lake Western Railroad Company, Subsidiary Debtor; State of Colorado; Colorado Public Utilities Commission; The United States Trust Company of New York, as Trustee; The Chase National Bank of the City of New York, as Trustee; The Chase National Bank of the City of New York; Guaranty Trust Company of New York, as Trustee; Central Hanover Bank and Trust Company, as Trustee; Untermeyer Family Group; General Securities Company; and Bankers Trust Company, as Trustee, Appellees

[fol. 243] OPINION—[May 10, 1945]

Before Phillips, Huxman, and Murrah, Circuit Judges.

William V. Hodges (F. C. Nicodemus, Jr.; Hodges, Vidal and Goree; and Pierce and Greer were with him on the brief) for Denver & Rio Grande Western R. Co., and Denver, Salt Lake Western R. Co.

Edward E. Watts, Jr., and Milton J. Keegan (Peter H. Holme; Mitchell, Capron, Marsh, Angulo and Cooney; and Dines, Dines and Holme were with them on the brief) for appellant City Bank Farmers Trust Company.

H. H. Larimore (J. W. Preston and R. L. Dearmont were with him on the brief) for appellant Guy A. Thompson, Trustee.

George D. Gibson and Henry W. Anderson (Grant, Shafroth and Toll; Hunton, Williams, Anderson, Gay & Moore; and Nan Ross McConnell were with him on the brief) for appellees Insurance Group Committee.

Norma L. Comstock; Alexander M. Lewis; and Rathbone, Perry, Kelley and Drye on the brief for appellee Central Hanover Bank and Trust Company, Trustee.

Edwin S. S. Sunderland (Pershing, Bosworth, Dick and Dawson; Davis, Polk, Wardwell, Sunderland and Kiendl; Thomas O. G. Fitzgibbon; and Judson C. McLester, Jr., were with him on the brief) for appellee Guaranty Trust Company of New York, Trustee.

James L. Homire (James A. Marsh and Emmet McCaffery were with him on the brief) for appellee Reconstruction Finance Corporation.

Lindsey and Larwill; Daniel K. Wolfe; and Stewart and Shearer on the brief for appellee United States Trust Company of New York, Trustee.

Lewis and Grant; Milbank, Tweed and Hope; and Arthur A. Gammell on the brief for appellee The Chase National Bank of the City of New York, Trustee.

[fol. 244] HUXMAN, Circuit Judge, delivered the opinion of the court.

The Denver and Rio Grande Western Railroad Company[1] and the Salt Lake Western Railroad Company, the second debtor,[2] filed their petitions in the United States District Court for the District of Colorado November 1, 1935, for reorganization under Section 77 of the Bankruptcy Act of July 1, 1898, as amended, 11 USCA, § 205. The petitions were approved on the same day, trustees were appointed, and the Debtor was authorized and directed to maintain and operate its property under this proceeding. The Debtor has now been in court under this proceeding for nearly ten years. The Debtor had outstanding numerous senior securities[3] which were secured by liens on various parts of the property embraced in the railroad system. These were preferred claims, superior in rank to all other claims against the Debtor. There are no issues or contests between the holders of these classes of securities and it is not necessary to treat them separately. They will be referred to collectively as Senior Bondholders. In addition to these bonds, the Debtor had outstanding general mortgage bonds, in the amount of $29,808,000, which were subordinate in rank only to the claims of the Senior Bondholders. They will be referred to as General Bondholders. The Debtor also had outstanding preferred stock and common stock.

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[1] Herein called the Debtor.

[2] The property of the second debtor became a part of the system property under the plan of reorganization. No separate questions arise by virtue of this debtor, and reference to it will not be necessary in the course of the opinion.

[3] These securities were as follows (not including certain bonds pledged to R. F. C. or Chase Bank to secure their notes hereinafter mentioned):

$15,190,000 Rio Grande Western first mortgage 4's.
15,080,000 Western Consolidated 4's.
2,000,000 Rio Grande Junction First 5's.
34,125,000 Denver Rio Grande Consolidated 4's.
6,382,000 Denver & Rio Grande Consolidated 4½'s.
12,000,000 Refunding and Improvement 5's.
2,000,000 Refunding and Improvement 6's.
A note to the Chase National Bank for $1,500,000.
Notes to the R. F. C. in the total sum of $10,691,850.
And equipment obligations in the sum of $2,325,000.

The contest in this case arises between the holders of securities of different rank or priority, by virtue of the fact that the total capitalized value found by the Commission for [fol. 245] the reorganized company is insufficient to satisfy in full all claims against the Debtor. The plan of reorganization under consideration satisfied in full the claims of the Senior Bondholders, by assigning to them new securities and common stock for the full amount of their claims. There was left common stock of the Debtor sufficient only to pay ten per cent of the claims of the General Bondholders, and nothing for the holders of the preferred stock and of the common stock. Their claims were adjudged worthless and they were barred from participating in the assets of the reorganized company.

Ten different plans of reorganization were proposed and considered by the Commission prior to the plan which was finally adopted and which is in controversy herein. Two plans were submitted to become effective January 1, 1937. One placed a valuation on the property of $149,732,966, and the other a valuation of $158,747,766. Both gave the General Bondholders 100 per cent of the value of their claims in new stock. Thereafter seven other plans were proposed. They gave the General Bondholders from 32.99% to 50% of their claims in new stock. The valuation placed on the Debtor's property in these plans varied from $135,005,436 to $161,631,934. The Interstate Commerce Commission submitted a third plan, effective January 1, 1942, which gave the General Bondholders five per cent of their claims in new stock. It valued the property at $142,846,612. Thereafter the Interstate Commerce Commission submitted a fourth plan, which is the one under consideration here. This plan is in the alternative. One provides for consolidation with the Denver and Salt Lake Railroad Company. The alternative does not provide for such consolidation. In the event of consolidation, the capitalized valuation placed on the property was $155,173,127. If there was no consolidation, then the capitalized valuation was fixed at $143,528,027. As stated, this plan gave the General Bondholders only ten per cent of the value of their claim in common stock, and barred the preferred stockholders and the common stockholders from participation in the reorganized company. For the purpose of the questions presented by this appeal, it is immaterial which valuation is considered.

On May 1, 1943, after the final plan, as outlined above, had been approved by the Commission, the Debtor filed a petition [fol. 246] with the Commission requesting that the proceedings be reopened for the introduction of additional evidence pertaining to the then existing economic conditions and the prospective earnings of the new company as they might affect the capitalization of the new company, the value of the property, and other elements of the plan. The Commission found that such additional evidence was not required and denied the petition. Thereafter the proposed plan was submitted to the District Court for its consideration.

On September 16, 1943, while the court had the plan under consideration, it entered an order providing that the Junction Bonds,[4] for which provision had been made in the capital structure, be paid from surplus cash in the hands of the Debtor's trustees. On October 25, 1943, the court entered an order approving the plan. Thereafter, on March 31, 1944, the trustees of the General Bonds filed an application with the District Court for a redistribution of the securities which had been set apart in the capital structure for the Junction Bonds. On April 26, 1944, the Commission submitted the plan to the creditors for acceptance or rejection. The General Bondholders rejected the plan by a vote of 20.67% for to 79.33% against the plan. The result of this vote was certified to the District Court. On November 29, 1944, the District Court entered a final order overruling the objections to the confirmation of the plan and denying the application for a redistribution of the securities set up for the Junction Bonds, and confirmed the plan. Appeals have been prosecuted both from the order of October 25, 1943, approving the plan, and from the final order of November 29, 1944. Both appeals present the same questions and they will not be separately treated. The questions urged by the various appellants will be considered without reference to the appellant presenting them.

Numerous assignments of error are urged by the various parties. They may be summarized generally as follows:

1. The Commission employed fundamentally erroneous methods of valuation in valuing the property of the new company.

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[4] The facts concerning these bonds will be developed later.

[fol. 247] 2. The Commissioner erred in denying the petition of the Debtor asking that the case be reopened for the consideration of additional evidence pertaining to the then existing economic conditions and the prospective earnings of the new company as they might affect the capitalization of the new company.

3. The plan is not fair and equitable and fails to afford due recognition to the rights of all classes of creditors and discriminates unfairly in favor of the Senior Mortgage Bondholders, within the meaning of Sec. 77(e) of the Act.

4. The rejection of the plan by 77% of the General Mortgage Bondholders, voting at an election for that purpose, deprived the court of the power to approve and confirm the plan.

5. The court erred in refusing to redistribute the securities intended for the Junction Bonds when they were paid from cash, so as to give the benefit thereof to the General Bondholders.

Method of Valuation

The Act provides that in valuing the property, the Commission shall give due consideration to earning power, past, present, and prospective, as well as all other relevant facts.[5] While the Commission's report recites that it gave consideration to all relevant factors, it must be conceded that the valuation was fixed almost entirely on the basis of earning power of the property.

Reproduction cost new less depreciation, and invested capital were stressed in the oral argument as fundamentally correct methods of valuation which must be considered as factors and taken into account in any proper valuation of a utility property. It is urged that the valuation of the Commission is fundamentally erroneous because these factors were disregarded.

A railroad is a utility, impressed with a public interest. The very existence of our nation depends upon a sound, efficient, transcontinental transportation system. The purpose of Section 77 is to provide an efficient and speedy

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[5] 11 USCA § 205(e).

[fol. 248] method of reviving sick and ailing railroads. It recognizes the rights of creditors and stockholders of the road. It preserves their interests in the property and maintains the rank and priorities of various classes of creditors. In addition to all this, it seeks to reorganize the road, to place it on a sound financial footing, so that it may continue to operate and serve the nation's needs.

The effective administration of Section 77 requires a reexamination and revaluation of the property of the railroad system. The primary question for the Commission is what value can be established upon which the road may expect to earn a reasonable return. Prospective earnings is a proper method by which to determine the new valuation of a railroad. In fact, it is the only method which can insure the continued operation of a railroad without recurring receiverships. The use of any method that does not reflect earning power is but a stop-gap on the road to bankruptcy. To provide that the new capitalization should not be less than the cost of reproduction new less depreciation, or not less than the capital investment would in itself be of no benefit to junior creditors if such value bore no sound economic relation to prospective earnings, because the earnings would be insufficient to pay their claims, and in the end their new securities would be as valueless as their present ones now are.

In Ecker v. Western Pac. R. Co., 318 U. S. 448, and Group of Investors v. Milwaukee R. Co., 318 U. S. 523, the Supreme Court definitely placed its stamp of approval upon prospective net earnings as a proper method of valuing a railroad in a reorganization proceeding under Section 77. In the Milwaukee case, the Supreme Court said:

> "The basic question in a valuation for reorganization purposes is how much the enterprise in all probability can earn."

The court points out that a disregard of that method of valuation can bring only a harvest of barren regrets. The court also points out in the Milwaukee case that the Commission may disregard other methods of valuation if in its opinion they afford no reasonable basis for believing that the probable earning power of the road is greater than [fol. 249] what the Commission had found by considering the prospective earnings. This all sums up to the conclu-

sion that earning power is the factor around which a reorganization must be built. We find no error in the use by the Commission of prospective earnings as the method of valuing the property of the Debtor.

It is urged that in any event the action of the Commission was arbitrary because it considered earnings only during the depression years and gave no regard to present or prospective earnings. This is not borne out by the record. The Commission reviewed and considered the earning history of the Debtor for the past 24 years. This included normal years and depression years, as well as abnormal war years. From all of this the Commission estimated the probable prospective earnings and based its valuation thereon. It is true that it did not give much consideration to the present inflated war earnings. For this it cannot be criticized. These earnings are to a great extent artificial, and will disappear largely with the coming of the peace. They have very little value in estimating the probable future earnings of this property in the peace economy which is to come. The Commission was well within its right in largely disregarding them in reaching its conclusions as to the probable prospective earnings of the property. See Group of Investors v. Milwaukee R. Co., supra, page 544.

It is further urged that the Commission fell into reversible error in failing to take into account new war industries which have been erected at various points on the system. Such industries have been erected and are operating as a part of our war economy. Who can now say how many of those, if any, will remain after the war and will continue to contribute to the income of the Debtor? Such factors are in the outer realm of speculation. No one can say with any degree of certainty what their future place in the economic world will be. Neither can it be said with any degree of sureness how much, if any, net revenues these industries will contribute to the system. In this situation it cannot be said the Commission erred in refusing to give such factors a prominent place in the capitalized value of the system based on prospective earnings. It did consider all of these factors, and from a view of the entire field, reached its conclusion as to the probable prospective earning capacity of the system.

[fol. 250] It is urged that the plan is fatally defective because the Commission refused to capitalize the excess

surplus current assets and thus make available more new securities for the General Bondholders. As of December 31, 1935, the Debtor had a deficit in its net working capital account of $9,727,230. December 31, 1942, the effective date of the plan, its net working capital was $6,811,077. December 31, 1943, the net working capital had increased to $10,398,084, and by December 31, 1944, the surplus had risen to $12,125,863.50. From this it will be observed that there was on hand an unusually large amount of current assets. We have already held that the Commission was on sound ground in giving little consideration to war profits in considering future prospective earnings. By the same reasoning, it was well within its rights in refusing to capitalize them and set them up as a part of the permanent capital structure of the company.

It is urged that the valuation of the Commission is fatally defective because it does not reflect extensive and valuable additions and betterments which were made by the trustees in this proceeding. At least since 1939 the Debtor has enjoyed substantial net income. The trustee's annual reports show that since the institution of this proceeding, the Debtor's net earned income has exceeded $50,000,000, and that more than $43,000,000 of this has been used in making permanent betterments and improvements. Many of such improvements substantially increased the potential earning capacity of the railroad. To illustrate: central train control was installed in many segments of the road where the greatest density of traffic obtained, thereby giving to such sections of the road the equivalent of a double track road. All of this has resulted in greatly increasing the efficiency and economy in the handling of traffic. It is true that as a result of these vast expenditures of the net earnings, the railroad has been greatly improved and the present owners will be handed a substantially new railroad system.

It is also true that the valuation adopted by the Commission does not reflect these improvements in the sense that the valuation was substantially increased over the value which had been placed on the property prior to the [fol. 251] time these improvements were made. But this in itself does not condemn the action of the Commission. The question for its determination was the earning capacity of this property. These improvements were considered by the Commission, and no doubt taken into ac-

count, together with all the other facilities of the road, in reaching its conclusion as to what the property reasonably could be expected to earn. It is not unreasonable to assume that if these improvements had not been made, the probable earning capacity would have been substantially reduced. This in turn would have resulted in a reduced valuation, which in turn would have reduced the participation of the General Bondholders in the reorganized company. It cannot be said, therefore, as a matter of law, that the General Bondholders will not receive some benefit from these expenditures. Whether these funds were wisely or equitably used for the benefit of all classes of creditors is not an issue in the present posture of the case. The question still is, does the valuation of the Commission bear reasonable relation to the prospective earning capacity of the road; and is the action of Commission in setting up the capital structure free from legal infirmities which require us to reject the plan?

It is also urged that the Commission erred in refusing to reopen the proceedings for the introduction of additional evidence pertaining to the then existing economic conditions and to the prospective earnings of the Debtor as reflected by the 1943 income. The record reveals that there was a substantial increase in the earnings of 1943 over 1942, but it is also shown that the increased cost of operation more than offset this increase and that the net income for 1943 was less than for 1942. This further evidences the difficulty in basing a valuation upon distorted conditions resulting from an all-out effort in a global war. This case has been before the Commission and before the court for nearly ten years. During all this time, all factors have been continuously considered, valuations have been made and rejected, and other valuations have been made. There must come a time when the matters should be determined and the proceedings closed. There was no reversible error in the refusal of the Commission to reopen the proceedings for further consideration of these matters.

It is settled beyond the question of a doubt by the deci- [fol. 252] sions of the Supreme Court in Ecker v. Western Pac. R. Co., and Group of Investors v. Milwaukee R. Co., supra, and in the special concurring opinions of Justice Roberts in those cases, that the duty of formulating a plan of reorganization under Section 77, including the adoption

of a new valuation of the property, is a function confided to the Interstate Commerce Commission, and that no court of law may interfere with such plan or valuation because it does not agree with it. The members of the Interstate Commerce Commission are skilled and well versed by long experience in the handling and determination of such problems, and Congress wisely charged them with the primary responsibility of administering the reorganization of railroads under Section 77. Courts may interfere with the capital structure or valuation made by the Commission in a proceeding under this Act only when it can be said as a matter of law that the Commission used fundamentally erroneous methods of valuation or acted arbitrarily or capriciously. An examination of the entire record leads to the conclusion that the action and the conduct of the Commission in fixing the valuation and setting up the capital structure is free from these infirmities, and that its action in relation thereto must be upheld.

As pointed out, Congress in passing Section 77 intended to place the reorganization of railroads largely under the jurisdiction of the Interstate Commerce Commission, with limited power of review in the federal courts. Aside from the limited power of review of the valuation by the Commission and of the plan of reorganization to see that they conform to constitutional requirements, the primary function to be performed by the courts is provided for in Section 77(e). Under this section it is the duty of the District Court to examine the plan to see whether it complies with Subsection (b), and whether it is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the various classes of creditors and stockholders. If the court is satisfied that these requirements have been met, it must approve the plan, otherwise it should disapprove and return it to the Commission for further consideration.

[fol. 253] As already pointed out, the District Court performed this function. It considered the plan, approved it in its order of October 25, 1943, and confirmed it in its order of November 29, 1944. On appeal, our scope of review is more limited than even that of the District Court. We inquire only to ascertain whether the District Court per-

formed its judicial functions under Subsection (c) and whether its conclusions find support in the record. We may not reverse the District Court merely because we would have reached a different conclusion. As stated by the Supreme Court, "If there is warrant for the action of the District Court, our task on review is at an end." Group of Investors v. Milwaukee, supra.

It is urged that there is no warrant in the record for the District Court's finding that the plan is fair and equitable and affords due recognition to the rights of all classes of creditors. The District Court found that the findings of fact by the Commission were supported by evidence and the findings of the Commission were accordingly adopted by reference as the findings of fact of the court.

In considering whether the plan is fair and equitable, affords due consideration to the rights of each class of creditors, and whether it does not discriminate unfairly in favor of one class at the expense of another, our problem is to determine whether within the framework of the capital structure set up by the Commission the assets have been distributed to the various classes of claimants within the rule of Northern Pac. Ry. v. Boyd, 228 U. S. 482, and Consolidated Products Co. v. DuBois, 312 U. S. 510. These cases merely reiterate the well established equitable rule that property of an insolvent corporation must be used to satisfy in full the claims of various classes of creditors according to their priority in rank.

It is not claimed that of the securities issued under the capitalization authorized by the Commission, more has been set over to the Senior Bondholders than is required to satisfy their claims in full, with the exception of the items hereinafter noted. But the argument is made that the capitalization should be increased by virtue of the permanent improvements made from net earnings during the receivership and by virtue of the large amount of current assets so as to afford more securities or common stock for [fol. 254] the General Bondholders. We have already disposed of the contention that the earnings which were invested in permanent improvements and betterments should be reflected in increased capitalized value, and nothing further needs to be said on this point.

The mere fact, however, that cash and current assets are not required to be reflected in the capital structure in the

form of capitalized value does not remove them from the picture. They are nevertheless, assets of the corporation which must be taken into account in drawing up a fair and equitable plan of reorganization, and must be distributed in a manner that is fair and equitable to all classes of creditors. The Senior Bondholders were paid in full. They received all the new securities and most of the common stock. Ninety per cent of the General Bondholders' claims were wiped out. They received only a small amount of common stock, ten per cent of their total claim.[6] Adequate operating funds are essential to the operation of a railroad. The Senior Bondholders were entitled to receive in addition to the full amount of their claims, working capital sufficient for proper and efficient operation of the railroad. But anything in excess of what was reasonably necessary for this purpose constituted assets of the insolvent corporation which belonged to the remaining creditors.

We think it is apparent from the record that there were current assets on hand consisting of cash and securities in excess of what was needed for the efficient operation of the road. As pointed out, the working capital of the debtor had increased from a deficit of $9,727,230 as of December 31, 1935, to a surplus of $12,125,863.50 as of December 31, 1944. While these increased net earnings are due in large part to the war and will not continue after the end of the war, and may therefore be disregarded in setting up the capitalized structure based upon prospective earnings, we cannot disregard the fact that these huge surpluses actually exist. Their existence is an accomplished fact. It is also obvious that surpluses will continue to pile up for a reasonable time yet to come. We think any plan which fails to take this into account and which gives the Senior Bond- [fol. 255] holders their claims in full by substantially delivering the road to them, and gives them the surplus cash actually on hand and further enables them to receive in addition the excess war profits which are reasonably sure to come, is inherently inequitable and unfair, so long as there are classes of creditors whose claims are not fully satisfied.

The appellees urge that we must view the picture as of

[6] For the purpose of developing this point, the Senior Bondholders will be treated as the new owners of the railway system.

June 14, 1943, and that at such time there were no surplus current assets on hand. The conclusion is inescapable that on either June 14, 1943, or December 31, 1943, there were on hand surpluses greatly in excess of what was necessary for the proper operation of the railroad. The Commission was cognizant of the fact that surpluses were accumulating from war profits. Throughout its deliberations, it discussed excess war earnings. The trial judge, who was operating the road under the bankruptcy proceedings, and who had intimate knowledge of the financial status of the Debtor, recognized that excessive current assets had accumulated. In his order of September 13, 1943, directing the payment of the Junction Bonds in cash, the court said: "The trustees having on hand an amount of cash *far in excess* of the needs of reorganization expenses, including working capital . . . ."

The inherent weakness in the plan was not only that it did not make equitable distribution of the excess current assets on hand, but also that it failed to provide for the equitable distribution of excess war profits which could reasonably be expected to accrue during the rest of the war period. This is especially significant in view of the complaint by the General Bondholders of the use which was made of the net earned profits during the period of the trusteeship.

They complain that practically all the net profits were used in making over the road instead of paying debts and that as a result debts mounted to a point where their equity in the property decreased from a 100 per cent participation in the capitalized structure under the first plan to a mere 10 per cent under the final plan. That they have a real grievance is apparent from the record.

On November 1, 1935, the Debtor's total debts senior to the claim of the General Bondholders was slightly over [fol. 256] $101,000,000. The General Bondholders' claims at that time were approximately $30,000,000, making the total of the two claims approximately $131,000,000. Any one of the ten plans of reorganization prior to the final one fixed the value of the property at more than enough to satisfy the claims of all bondholders in full, as of the date this proceeding was instituted. During the ten intervening years, the claim of the Senior Bondholders increased to more than $139,000,000, and that of the General Bond-

holders to more than $43,500,000, making a total of more than $482,000,000, required for the two classes of claims.

During all of this period the Debtor enjoyed substantial income, amounting to approximately $50,000,000. Instead of using this income in payment of interest on the senior claims, it was used in making permanent and lasting improvements in the road. More than $43,000,000 was used in this way. None of these expenditures has resulted in a comparable increase or in any substantial increase in the final valuation, over the valuation prior to the making of the improvements. But as a result of this operation, the position of the General Bondholders has deteriorated from a 100 per cent participation of the amount of their claims to a mere ten per cent. Nor does it change the picture to say that these improvements were necessary to the railroad system. The fact still remains that earnings in which all had a vital interest were used in building a new railroad in many respects, which will be handed over to the Senior Bondholders, and the General Bondholders will practically be eliminated as a result thereof.

But this alone does not entitle the General Bondholders to a greater participation in the reorganized company. Neither does it condemn the plan of reorganization or the capital structure set up therein. The operation of a railroad involves the expenditure of large sums for operation. It involves the formulation of plans of operation and the exercise of judgment and discretion. If, in the exercise of this discretion, funds are unwisely spent, from the viewpoint of the interest of all creditors, they may feel aggrieved, but they have no legal cause of complaint.

Neither was the Commission compelled to, nor would it [fol. 257] be justified in adding the amount of these expenditures to the capitalized value if in the exercise of sound discretion it felt that the reasonable prospective earnings of the road after the improvements did not justify it. However, in the face of all this, after satisfying in full the claims of the senior bondholders, the plan of reorganization should have made sure that all excess current assets, as well as all excess war profits yet to accrue, would go to the General Bondholders.

The commission, as pointed out, adopted a conservative, sound estimate of the prospective earnings of the reorganized company. For this it is not to be criticized. An over-

optimistic view would again surely lead the Debtor into the bankruptcy courts, with which it has had too much acquaintance already.[7] We, however, feel that there is more than a speculative probability that these war industries which have been constructed along the system, as well as the improvements which have been made by the use of these net earnings, might produce greater net returns than anticipated in the plan. If such should be the case, they certainly belong to the General Bondholders and not to the Seniors, and the plan should bring this about. It could be done by issuing to the General Bondholders an additional amount of a subordinate stock which would receive returns only from excess dividends. This is a mere suggestion on our part, and in no wise binding on the Commission. Our duty is limited to pointing out defects in the plan. It is the responsibility of the Commission to correct them.

The Junction Bonds

We think that the complaint as to the manner in which the Junction Bonds were handled is well taken. The Rio Grande Junction Railroad is a wholly owned subsidiary of the Debtor. It had bonds outstanding in the hands of the public for the payment of which the Debtor was liable, totaling $2,758,333. This claim was senior to that of the [fol. 258] General Bondholders. The plan set aside securities for the payment of this claim. In an order dated September 13, 1943, the District Court directed the trustee to pay this claim with some of the surplus cash on hand, and retained the securities which were to be used in the payment thereof in the treasury of the company. The court treated the transaction as a purchase of securities rather than a payment of a debt. This is a play upon words, and, in any event, is immaterial to the issue. The fact remains that the new capitalization provided securities for the pay-

[7] Properties included in this railroad system have participated in the following reorganizations: The Denver & Rio Grande R. Co. was a successor in a reorganization proceeding in 1886; the Rio Grande & Western R. Co. was the successor in a reorganization proceeding in 1889; these two companies consolidated in 1908 under the name of the Denver & Rio Grande R. Co.; the present company was reorganized in 1920 and again in 1922 to 1924.

ment of these bonds. The value behind these securities in no wise belonged to the Senior Bondholders, because they had been paid in full. When surplus cash was used to pay this claim, the value behind the securities set aside for that purpose remained undistributed. Since the Senior Bondholders had been satisfied in full, this undistributed value in all equity and fairness belonged to the General Bondholders. Any plan which does not give it to them does not comply with the requirements of Section 77(e) of the Act.

Decrease in Senior Debt

Debts due to the senior creditors, which are all classified in this opinion as Senior Bondholders, included equipment obligations of $5,758,000. Under the plan, these claims are to be paid with new securities and are thus satisfied before the General Bondholders receive anything. As of December 31, 1944, the equipment obligations had been reduced to $4,540,000.[8] This resulted in a decrease in these obligations of $1,218,000. The new securities set apart for the payment of this sum will not be needed. If no further disposition is made of the securities provided for this debt, the value behind them will inure to the further benefit of the Senior Bondholders. What we have said with regard to the Junction Bonds applies with equal force here. It would be inequitable to give this additional value to the Senior Bondholders when they have already been fully compensated. This unused value belongs to the General Bondholders. This question has arisen since the adoption of the plan, and therefore cannot condemn the plan as it was [fol. 259] formulated and adopted, but since the proceedings must go back to the Commission, failure to take this change in Senior Bond requirements into account and make the capitalized value represented by these securities available to the General Bondholders would violate the requirements of Section 77(e).

Utah Fuel Company Stock

Complaint is also made of the manner in which the plan disposes of the capital stock of the Utah Fuel Company. The capital stock of this company consisted of 100,000

[8] See page 6, Income Account and Financial Exhibit, period ending December 31, 1944.

shares. All of it was pledged as collateral security for the payment of the first consolidated mortgage bonds of the Rio Grande Western Railway Company.[9] The Commission's amended order disposes of this collateral in the following manner; "* * * the trustee under the mortgage securing the R. G. Western Consolidateds [shall] be permitted to obtain the release of the equities * * * in the stock of the Utah Fuel Company, and distribute the stock among the holders of bonds in any manner acceptable to them, or to enforce its rights as pledgee of the stock, * * * [of the Utah Fuel Company] the proceeds recovered to be distributed to the holders of the bonds."

It is contended that the holders of the Rio Grande Western First Consolidated Mortgage Bonds should be compelled to either foreclose this collateral and apply the proceeds on their claim or should credit their claim with the value of this collateral and should then be allowed new securities for only the balance of their claim. It is contended that under the manner in which this collateral was treated, this class of claimants received more than full payment of their claim, at the expense of the General Bondholders.

There can be no question as to the duty resting upon these claimants to credit the value of this collateral upon their claim before sharing in the securities of the reorganized company. They were entitled only to full payment. If the new securities which were assigned to them satisfied their [fol. 260] claim in full, then the plan which permitted them to retain in addition this collateral would be inequitable and unfair to junior creditors.

The findings of the Commission are not clear as to the manner in which it treated this collateral. In its second supplemental report, of July 13, 1942, it states: "In our opinion, these bondholders are entitled to receive the beneficial interest in the Utah Fuel Company Stock in addition to the reorganization securities allotted to them." This language could be construed to mean that the Commission was of the opinion that it took this collateral, plus the new securities, to fully satisfy the claim of these creditors.

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[9] These obligations are a part of the claims referred to as the Senior Bondholders.

Neither does the record establish with any degree of satisfaction the value of this collateral. There is evidence which would support a conclusion that it had but little value. On the other hand, there is evidence that the Utah Fuel Company is now prosperous and is enjoying large earnings, with reasonable prospects that they will continue.

It appears to us that the plan contemplates that the claim of these creditors was to be satisfied from the new securities which were set apart for them, and that no particular value was ascribed to this collateral. If this collateral has any substantial value, it must be taken into account before the amount of new securities which are to be set over to these claimants is determined. The Commission should clear up the doubts and uncertainties which surround this matter when the proceedings are returned to it for further consideration.

It follows from what has been said that the General Bondholders were reasonably justified, within the meaning of the statute, in rejecting the plan, and that the District Court was without authority to confirm the plan in the face of their adverse vote.

Under the admitted facts of the case, whether the plan complies with the requirement of Section 77(e) presents a pure question of law, and we are in no wise bound by the legal conclusions of the District Court in this respect. It is our conclusion that the plan fails to meet the requirements of Section 77(e) in that it fails to make equitable distribu-[fol. 264] tion of the surplus cash and current assets on hand; fails to make equitable provisions for the distribution of the excess war profits which may reasonably be expected to accrue; fails to make equitable and fair distribution of that part of the capitalized value represented by the securities set aside for the Junction Bonds. It is suggested that the District Court has power to make an equitable redistribution of the value represented by the undistributed securities, and that it is not necessary to remand this issue to the Commission. In view of the other questions which must be considered by the Commission, we deem it unnecessary to pass upon this question. We think the interests of all parties can best be served by having the entire matter reconsidered by the Commission and have it make all necessary adjustments.

Not much has been said about the claims of the preferred stockholders and the owners of common stock. It is quite apparent that no valuation based upon any reasonable estimate of prospective earnings could be sufficiently large to pay them anything. The finding that their claims are valueless and the order barring them from participation in the plan of reorganization is approved.

For the reasons herein stated, the order of the District Court of October 25, 1943, approving the plan, and its order of November 29, 1944, confirming the plan, are hereby reversed and the cause is remanded with directions to enter an order disapproving the plan, and remanding the case back to the Interstate Commerce Commission for its further consideration.

> "Nothing in this opinion shall prejudice or foreclose the rights of the parties to propose a new plan of reorganization or the power of the Commission to formulate, approve, and certify a new plan of reorganization in the light of any relevant facts presented to the Commission in any proceeding under 11 U. S. C. Sec. 205(d)."

It Is So Ordered.

[fol. 262] PHILLIPS, Circuit Judge, concurring:

The broad language of the Supreme Court in the Western Pacific case and the Milwaukee case[1] compels me to conclude that we cannot disturb the Commission's finding of valuation nor the finding of the Commission, confirmed by the trial court, that the equities of the unsecured creditors and the preferred and common stockholders have no value. Nevertheless, I feel impelled respectfully to suggest that the elimination of a substantial portion of the claim of the holders of the general mortgage bonds and all of the claims of stockholders and unsecured creditors, on the basis of a valuation resting wholly on an estimate of future earnings, is harsh treatment of such claims. I say this because, while according expertness to the Commission, it is my opinion that such future earnings cannot be estimated with

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[1] Ecker v. Western Pacific R. Corp., 318 U. S. 448;
Group of Investors v. Milwaukee R. Co., 318 U. S. 523.

a degree of certainty that is not likely to result in grave injustice.

The injustice to junior security holders which may result from a valuation based solely on an estimate of future earnings has aroused the attention of Congress and corrective legislation has been introduced. H. R. 4960 has already passed the House and is pending before a Senate Committee.[2]

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[2] The House Judiciary Committee, in its unanimous report (78th Cong., 2d Sess., Report No. 1615) recommending passage of H. R. 4960, in part said:

> "The purpose of the bill is to correct a very serious situation arising from the interpretation placed by the Interstate Commerce Commission and the courts upon the amendments of section 77 enacted by the Congress August 27, 1935. We believe this situation results from a misapprehension of the intention of Congress with respect to the 1935 amendments. The consequences have been and are so disastrous to railroad investors, and so dangerous to the credit of the railroads in general, that they should be corrected by legislation.
>
> "From a legal standpoint, the problem may be stated simply. Section 77 was directed primarily to the relief of financially embarrassed railroad companies through a revision of their capital structures and a reduction of fixed charges. It does not expressly provide for any reduction in the existing total capitalization; but the Interstate Commerce Commission has interpreted paragraph (d) of the section as authorizing it to fix the total capitalization of the reorganized company. In so doing, it has estimated a 'capitalizable value of the assets' of the property based almost entirely upon 'earning power'—earning power of the property, past, present and prospective—as these words are used in section 77(e). Its estimates of prospective earning power are necessarily speculative. Nevertheless it has used its estimates of earning power to fix capitalizations in all cases very substantially below the existing capitalizations, regardless of the investment in the property and of the valuation previously determined by the Commission under section 19a of the Interstate Commerce Act. The Supreme Court in

[fol. 263] On November 1, 1935, during the depths of the national depression, the debtor came into court for reorganization. At that time the debtor's senior debts ahead of the general mortgage bonds aggregated slightly over $101,000,000 and the claim of the general mortgage bondholders aggregated about $30,000,000. With an immediate reorganization, a capitalization of $132,000,000 would have been [fol. 264] adequate to give the general mortgage bondholders new stock equal to 100 per cent of their claim. No capitalization or valuation ever proposed for the debtor, in any plan presented, has been that low. During the eight years' delay in reorganization (in nowise due to the general mortgage bondholders, but, at least in part, to controversies among the senior security holders) and up to January 1, 1943, the effective date of the plan, the claims of the senior security holders, due to the accrual and nonpay-

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passing upon two major reorganization plans—the Western Pacific and the Chicago, Milwaukee, St. Paul & Pacific—upheld the Commission in this interpretation of the section, and has further held that the Commission's findings will not be disturbed where there is some evidence to support them. In other words, these administrative findings are beyond judicial review.

"The result of this interpretation of the statute by the Commission, and the subsequent refusal of the courts to review the Commission's findings, has caused the destruction of hundreds of millions of dollars of railroad securities representing actual investment in the property made, to some extent at least, in reliance upon the belief that such investments could not be confiscated except by due process of law.

. . . . . .

"In five major companies now undergoing reorganization, the reductions in capitalization aggregate some $600,000,000, meaning that this amount of railroad securities has been eliminated in the reorganization of these five companies alone, although there is no question that the investment in road and equipment and the 19a valuations at the present time are far in excess of the capitalization determined by the Commission. The

ment of interest, increased about $38,000,000. The debtor's net income available for interest during the trusteeship to the end of 1944 amounted to $19,420,972. It exceeded by approximately $9,500,000 the interest charges which accrued on the claims of senior security holders to the end of that [fol. 265] year. As of December 31, 1935, the debtor's current assets were $9,727,239 less than its current liabilities. As of December 31, 1944, the debtor's current assets exceeded its current liabilities by $12,125,863.50. Thus it will be seen there has been a favorable change in the current situation of $21,853,093, and, moreover, since the plan was formulated, the Junction Bonds have been paid and equipment obligations have been reduced from $5,758,000, the amount provided for in the plan, to $4,540,000, a reduction in that requirement of $1,218,000.

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same is true generally of the other roads involved in reorganization, these five being specifically mentioned, because they are included in one exhibit submitted to this committee by the Interstate Commerce Commission (hearings on H. R. 2857, serial No. 9, p. 199).

"That this situation has created an unbearable hardship upon the junior investors in railroad securities and constitutes a real danger to railroad credit may be easily seen from a glance at current railroad earnings. In 1942 the Missouri Pacific earned $32.67 a share on the common stock outstanding under the old capitalization; the Denver & Rio Grande Western, $34.40 a share; Rock Island, $25.11; Frisco, $18.03; St. Louis Southwestern, $27.23. These figures approximately were repeated in 1943; and the high earnings are continuing in 1944. Yet these stocks, which have demonstrated such an earning power, have been absolutely wiped out in reorganization, and the stockholders are without remedy. Moreover, the junior securities of all these roads have been drastically cut in reorganization and the senior securities have been very largely converted into income bonds and preferred and common stock. In one case, the Commission estimated a normal earning power of $11,000,000, and based its capitalization upon that figure; yet in the same year in which the Commission's plan was announced (1941) that road earned more than $18,000,000. In 1942, it earned $36,000,000,

Approximately $43,000,000 of the income available, but not used, for the payment of interest has been expended in permanent improvements and betterments. While the investment value of the debtor's property thus was substantially increased, the Commission's valuation, based on estimated future earnings, was not increased proportionately. As a result, the claim of the senior security holders has increased, and the participation of the general mortgage bondholders has been pressed downward until it is now fixed at 10 per cent of the new common stock. Many of the improvements and betterments referred to above, have substantially increased the capacity of the railroad to handle increased traffic as it arises. Central train control installed in many segments, where the greatest density of traffic obtains, gives to those segments, in a large degree, the equivalent of a double-track railroad and increases the

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and in 1942 $37,000,000. Nevertheless the Commission still says the old common stock is worthless. The stockholders are without remedy. There is in practical effect no judicial review of the action of the Commission. Although its guesses as to future earning power has been demonstrated to be wrong, its findings are final.

* * * * * * * * *

"The primary purpose of the bill is to insure that the courts shall make an independent judicial review of each plan and of the evidence upon which the plan is based. Under the existing statute, the Commission is required to certify to the court a transcript of its proceedings; and the court is required to notify all parties and, if objections are filed, to have a hearing. The effect of the proposed amendments is to require the judge to make an independent judicial determination of the facts found by the Commission, and not to hold that the administrative finding of the Commission is beyond judicial review. With this object in mind, the bill provides that the judge shall not only be satisfied that the plan complies with the provisions of subsection (b) as in the present statute, but must also be satisfied that it complies with the provisions of subsection (d), which the Supreme Court held was not within the province of judicial review. This will add nothing to the require-

number of trains that can be operated over the road and the volume of traffic that can be handled by the road. Other of such improvements have contributed to efficiency and economy in operations. These improvements have enabled the debtor to handle the great increase in traffic resulting from war effort and have placed the debtor in a position to more economically and efficiently handle a volume of traffic largely in excess of its prewar traffic, should future economic conditions produce such traffic. Under the plan approved and confirmed by the district court, 90 per cent of the common stock goes to the holders of the senior securities and 10 per cent to the general mortgage bondholders. As a result, should there be a substantial increase in the debtor's postwar traffic over its pre-war traffic, 90 per cent of the increased earnings will inure to the benefit of the holders of the senior securities and only 10 per cent [fol. 266] to the general mortgage bondholders, whose claim was decreased 90 per cent by reason of the failure to discharge interest accruals with income available therefor and the diversion of such income to the cost of such

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ments of the present statute as to the hearing and the scope of the evidence; it will merely direct the courts to exercise the traditional right of review, and to give the parties and the public the benefit thereof.

"Second, and as a means of insuring that the Interstate Commerce Commission shall be guided by some standard in determining the permissible capitalization of the reorganized company, the bill provides that the existing total capitalization shall not be reduced below the lower of either the investment in the property or the physical valuation as previously determined by the Commission under section 19a. Naturally, if the existing capitalization exceeds the investment, it should be susceptible of reduction, if the Commission finds it is not supported by earning power; or, if the existing capitalization exceeds the physical valuation found by the Commission, it should be susceptible of reduction, unless in that event the Commission deems the earning power sufficient to support it. But where the existing capitalization represents actual investment in the property, or where it is not in excess of the value determined by the Commission under the mandate of law, then it should not be disturbed."

permanent improvements. It seems to me, under all these circumstances, that, in addition to the other adjustments required to make the plan fair and equitable, the Commission should endeavor to modify the plan so as to give relief from the situation that lets the full impact of the improvement program fall upon the claim of the general mortgage bondholders and accords them no corresponding benefits.

By confirming the finding of the Commission that the equities of the unsecured creditors and the stockholders are without value, based on an estimate of future earnings, an estimate at best shrouded in uncertainty, the court, by judicial fiat, has forever forfeited and destroyed the rights and interests of such creditors and stockholders in the assets of the debtor, a result which, under well-settled principles, a court of equity will ordinarily avoid.

It may be urged that the elimination of the stock will provide the debtor with a stronger financial structure and enable it to better serve the public interests, but private property cannot be taken in the public interest without just compensation.

Even if viewed solely from the standpoint of future earnings, it would seem that it should not be said such stock is without value merely because, during periods of receding economy and depression, the earnings of the debtor will not be sufficient, after payment of prior claims, to provide funds from which dividends on such stock can be properly paid. Such stock has value, if, during periods of expanding economy and property, the earnings of the debtor will be sufficient to provide for prior claims and leave a surplus from which substantial amounts can be lawfully paid as dividends thereon; and a finding of no value should not be made if there is reasonable probability that earnings will be realized from which substantial dividends can be paid, even though only during periods of economic prosperity.

[fol. 267] It seems to me, under the facts presented on this record and those of which we may take judicial notice, that it is not unlikely the estimate of future earnings of the debtor made by the Commission will fall far short of its actual future earnings. Should the estimated earnings prove to be substantially under the actual earnings, the injustice that will result to the holders of the general mortgage bonds and to the stockholders of the debtor is obvious.

It may be reasonably assumed that a substantial portion of the war industries contributing traffic to the road will be succeeded by permanent industries. For example, it is common knowledge that the Kaiser Industries and one of the large Eastern steel companies have indicated a desire to acquire and continue the operation of the Geneva Steel Plant, a large and modern steel plant built on the debtor's line of railroad. In the areas tributary to debtor's line of railroad, there is an abundance of cheap power and of fuel and ore. Many heavy traffic producing enterprises have been and are being established in new areas tributary to the debtor's line of railroad. It is reasonable to believe that this industrial development will continue.

Furthermore, changes in national income at constant prices have an approximately constant relationship to changes in ton-miles of traffic. It may be said, in general, that traffic is so related to national income that when that income rises by one billion dollars, traffic rises by about 6.6 billion ton-miles. Certain federal agencies have made estimates of the national income for the years 1947 to 1949. These estimates predict a national income of approximately 135 billion dollars in 1947 and a rising national income in 1948 and 1949, reaching 150 billion dollars in the latter year.[3] This would indicate a postwar railroad traffic reaching in 1949 a level of that traffic during 1943.

Moreover, the ratio between ton-mile revenue of Class I railroads and the number of factory workers engaged in the [fol. 268] production of durable goods is fairly constant. It is 100,000 revenue ton-miles for each factory worker. That there will be a determined effort to provide jobs for upward of 55 million workers early in the postwar period is a well-known fact. This indicates a greatly increased postwar railroad traffic. Moreover, the record demonstrates that, with the exception of a slight dip in 1923, the debtor has been securing a constantly increasing proportion of the operating revenues of Class I railroads. If the debtor should enjoy postwar earnings approximating its 1943 earnings, it is clear that the valuation found by

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[3] See Post-War Traffic Levels, prepared by Spurgeon Bell, Head Transport Economist, and L. E. Peabody, Principal Transport Economist, of the Interstate Commerce Commission, pp. 42-71, 90-114.

the Commission should be substantially increased. But, as suggested above, it is my conclusion that only through corrective legislation or a more liberal attitude on the part of the Commission can the junior security holders obtain relief.

[fol. 269] In United States Circuit Court of Appeals

Judgment—May 10, 1945

These causes came on to be heard on the transcript of the record from the District Court of the United States for the District of Colorado and were argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the order of the District Court of October 25, 1943, approving the plan, and its order of November 29, 1944, confirming the plan, are hereby reversed and the cause is remanded with directions to enter an order disapproving the plan, and remanding the case back to the Interstate Commerce Commission for its further consideration; and that appellants have and recover of and from appellees their costs herein.

[fol. 270] In United States District Court

Oral Opinion—Hearing had on September 14, 1943

"The Court: It seems to the Court that the recent decisions of the Supreme Court have not dealt specifically with what is to be done with the surplus cash resulting from the great increase in business that the railroads of this country have experienced during the war period.

This railroad has an amount of cash here that it is not necessary to carry forward into the reorganization; it is not necessary for the proper financing of the new company, and even if this two million dollars plus is paid, there would still be plenty of working capital to go ahead with under the plan.

I have old-fashioned ideas, perhaps, and in all receiverships in this court, where there are debts and assets to pay them, I believe in paying off one's debts; that that is the best financing there is.

I see nothing in the statute or in the plan which forbids this action. It has been admitted that the Court could have [fol. 271] paid this off before the plan came out, and I am not

convinced that the simple fact that the plan has been promulgated changes that situation, or the power of the Court to deal with this surplus cash.

My experience with this railroad in its previous receiverships indicates that if too much cash is turned over to the new company, it will be used not for the payment of debts but for the interests of the security holders or the public.

So the order of the Court will be that these Rio Grande Junction Bonds be paid, with interest. The amount would be a matter of accounting, and if counsel cannot agree upon that, the Court will discuss it later with them. But I believe that this two million dollars plus of bonds should be paid off, and an order to that effect may be made.

I believe the remedy for any complaint against the Court's action is by appeal, and I do not believe it requires the Court to send the plan back to the Commission of its own motion.

The railroads of America are being watched very carefully to see what disposition will be made of these tremendous earnings and surpluses that they are building up. If they are used wisely and providently for the purpose of reducing their heavy load of indebtedness, all will be well; otherwise they invite more radical legislation of a nature that will affect the railroad security holders to a far greater degree than any plan that the Commission or the Court can compel them to take.

Mr. Gibson: If the Court please, with that ruling and order, may I ask your Honor whether you would consider reaching that result by way of purchase rather than a payment, in order to avoid serious income taxes?

The Court: Yes, you may make the order in any way so that it will avoid taxes or most convenient in considering these incidental questions that may arise. I shall be glad to consider it when the order is drawn. Is there anything else before we get down to the plan?

[fol. 273] IN UNITED STATES DISTRICT COURT

ORDER (No. 484) FOR PURCHASE OF JUNCTION BONDS—Filed September 16, 1943

This matter came on further to be heard at this term, and was argued by counsel, and, thereupon, upon consideration thereof, it was

ORDERED:

1. The Trustees of the Debtor, The Denver and Rio Grande Western Railroad Company, are hereby directed, out of the cash funds in their hands as Trustees, to purchase for the benefit of the trust estate the First Mortgage 5% Bonds due December 1, 1939 of The Rio Grande Junction Railway Company, at the principal amount thereof and the unpaid interest thereon computed at the rate of 5% per annum to the date when funds are made available for such purchase.

2. Said Trustees are directed to give not less than two weeks' notice of the time and place at which holders of said Bonds may present their Bonds for sale to such Trustees, and of the terms thereof, by publishing at least once in a newspaper published and of general circulation in the City of Denver, Colorado and at least once in one or more newspapers published and of general circulation in the City of New York, New York a notice in substantially the following form:

> "To Holders of The Rio Grande Junction Railway Company First Mortgage 5% Bonds due December 1, 1939;
>
> NOTICE is hereby given that, pursuant to order of the U. S. District Court for the District of Colorado, the undersigned will, on and after ——, 1943, purchase the above-described bonds, at the price of $— per $1,000 bond, such price representing the principal [fol. 274] amount of each of said bonds, together with interest thereon from June 1, 1935 to ——, 1943 computed at the rate of 5% per annum.
>
> Holders of said bonds may deliver the same and receive the purchase price, on or after ——, 1943, at the office of Central Hanover Bank and Trust Company, 70

Broadway, New York (as agent of the Trustees), or at the office of the Trustees in Denver, Colorado, bonds in coupon form to be accompanied by the coupons maturing on December 1, 1935 and subsequently, and registered bonds to be accompanied by duly executed instruments of transfer.

Wilson McCarthy, Henry Swan, Trustees of The Denver and Rio Grande Railroad Company."

3. The said Trustees shall hold said Rio Grande Junction Railway Company First Mortgage 5% bonds, when acquired by them, subject to the further order or orders of the Court, and the Court reserves full jurisdiction to determine the disposition to be made of such bonds and of all interests therein, and of all questions arising from their acquisition.

J. Foster Symes, United States District Judge.

Denver, Colorado, September 16th, 1943.

[File endorsement omitted.]

[fol. 275] In United States District Court

Certificate of Interstate Commerce Commission—Filed July 15, 1944

Interstate Commerce Commission, Washington

Finance Docket No. 11002

The Denver and Rio Grande Western Railroad Company Reorganization

Summary of Certificate

July 4, 1944.

Pursuant to its order of March 23, 1944, the Commission, division 4, on April 26, 1944, submitted for acceptance or rejection by creditors of classes 6, 7, 8, 10(a), 10(b), 11, 12(a), and 12(b) of The Denver and Rio Grande Western Railroad Company, and by creditors of classes 1 and 2 of The Denver and Salt Lake Western Railroad Company,

as therein provided, the plans of reorganization of The Denver & Rio Grande Western Railroad Company, debtor, and of The Denver and Salt Lake Western Railroad Company, subsidiary debtor, approved by the Commission by its third supplemental report and order of June 14, 1943, and approved by the District Court of the United States for the District of Colorado on October 25, 1943. The results of the voting on the basis of the principal and interest of the claims voted, are summarized in the following tabulation,

Class	Per cent of Total Vote Accepted	Rejected
6. Holders of The Denver & Rio Grande Railroad Company's first consolidated bonds	99.29	0.71
7. Holders of The Rio Grande Western Railway Company's first-trust mortgage bonds	99.74	0.26
8. Holders of The Rio Grande Western Railway Company's first consolidated mortgage bonds	99.53	0.47
10(a) Holders of the debtor's refunding and improvement mortgage bonds (Series A)	80.00	20.00
10(b) Holders of the debtor's refunding and improvement mortgage bonds (Series B)	95.88	4.12
11. Holders of the debtor's general mortgage bonds	20.67	79.33
12(a) Reconstruction Finance Corporation; holder of debtor's secured notes	100.00	
12(b) Chase National Bank of the City of New York, holder of debtor's secured note	100.00	
1. Holder of The Denver and Salt Lake Western Railroad Company's common stock	100.00	
[fol. 276] 2. Reconstruction Finance Corporation, holder of The Denver & Salt Lake Western Railroad Company's secured note	100.00	

[fol. 277] Certificate

At a Session of the Interstate Commerce Commission, Division 4, held at its office in Washington, D. C., on the 4th day of July, A. D. 1944.

Finance Docket No. 14002

The Denver and Rio Grande Western Railroad Company
Reorganization

The Commission, division 4, having on April 26, 1944, pursuant to its order of March 23, 1944, in this proceeding, submitted for acceptance or rejection by creditors of classes 6, 7, 8, 10(a), 10(b), 11, 12(a), and 12(b) of The Denver and Rio Grande Western Railroad Company, and by creditors of classes 1 and 2 of The Denver and Salt Lake Western Railroad Company, as therein provided, the plans of reorganization of The Denver and Rio Grande Western Railroad Company and of The Denver and Salt Lake Western Railroad Company approved by the Commission by its third supplemental report and order of June 14, 1943, and approved by the District Court of the United States for the District of Colorado having jurisdiction of the proceedings for reorganization of the debtor, by order of October 25, 1943.

It is hereby certified, That proper ballots for acceptance or rejection of the plan were transmitted, within the time specified in the order of March 23, 1944, by creditors of class 6, holding $21,739,000, principal amount, of The Denver & Rio Grande Railroad Company first consolidated mortgage bonds, out of a total of $40,507,000, principal amount, of such bonds outstanding; by creditors of class 7, holding $9,499,000, principal amount, of The Rio Grande Western Railway Company first trust mortgage bonds, out of a total of $15,190,000, principal amount, of such bonds outstanding; by the creditors of class 8, holding $9,166,000, principal amount, of The Rio Grande Western Railway Company first consolidated mortgage bonds, out of a total of $15,080,000, principal amount, of such bonds outstanding; by the creditors of class 10(a), holding $1,000,000, principal amount; of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage six-percent series A bonds, out of a

total of $2,000,000, principal amount, of such bonds outstanding; by the creditors of class 10(b), holding $4,500,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage five-percent bonds, series B, out of a total of $12,000,000, principal amount, of such bonds outstanding; by the creditors of class 11, holding $6,443,150, principal amount, of The Denver and Rio Grande Western Railroad Company general mortgage bonds, out of a total of $29,808,000, principal amount, of such bonds outstanding; by the Reconstruction Finance Corporation, sole creditor of class 12(a), holding secured notes of The Denver and Rio Grande Western Railroad Company in the principal amount of $7,581,000; by the Chase National Bank of the City of New York, sole creditor of class 12(b), holding a secured note of The Denver and Rio Grande Western Railroad Company in the principal amount of $1,500,000; by the trustees of The Denver and Rio Grande Western Railroad Company, voting as representatives of that company as sole stockholder of class 1 of The Denver and Salt Lake Western Railroad Company, for the entire outstanding 36,310 shares of common stock of that company; and by [fol. 278] the Reconstruction Finance Corporation as sole creditor of class 2 of The Denver and Salt Lake Western Railroad Company, holding a secured note of that company in the principal amount of $3,110,850.

It is further certified, That defective ballots, hereinafter more specifically described, were transmitted within the time specified in the order of March 23, 1944, by other creditors of class 6, holding $355,500, principal amount, of The Denver & Rio Grande Railroad Company first consolidated mortgage bonds; by other creditors of class 7, holding the $138,000, principal amount, of The Rio Grande Western Railway Company first trust mortgage bonds; by other creditors of class 8, holding $38,000, principal amount, of The Rio Grande Western Railway Company first consolidated mortgage bonds; by other creditors of class 10(b), holding $382,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage bonds, series B; and by other creditors of class 11, holding $287,200, principal amount, of The Denver and Rio Grande Western Railroad Company general mortgage bonds outstanding.

It is further certified, That creditors of class 6, holding $21,585,000, principal amount, of The Denver & Rio Grande Railroad Company first consolidated mortgage bonds, constituting (with accrued interest) 99.29 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that creditors of that class holding $154,000, principal amount, of the bonds, constituting (with accrued interest) 0.71 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That creditors of class 7, holding $9,474,000, principal amount, of The Rio Grande Western Railway Company first trust mortgage bonds, constituting (with accrued interest) 99.74 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that creditors of that class holding $25,000, principal amount, of the bonds, constituting (with accrued interest) 0.26 percent of the total of allowed claims of that class voting on the plan rejected the plan.

It is further certified, That creditors of class 8, holding $9,123,000, principal amount, of The Rio Grande Western Railway Company first consolidated mortgage bonds, constituting (with accrued interest) 99.53 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that the creditors of that class holding $43,000, principal amount, of the bonds, constituting (with accrued interest) 0.47 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That creditors of class 10(a), holding $800,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage six-percent series A bonds, constituting (with accrued interest) 80.0 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that the creditors of that class holding $200,000, principal amount, of the bonds, constituting (with accrued interest) 20.0 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That creditors of class 10(b), holding $4,401,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and im-
[fol. 279] provement mortgage five-percent series B bonds, constituting (with accrued interest) 95.88 percent of the

total of the allowed claims of that class voting on the plan, accepted the plan, and that the creditors of that class holding $189,000, principal amount, of the bonds, constituting (with accrued interest) 4.12 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That creditors of class 11, holding $1,332,050, principal amount, of The Denver and Rio Grande Western Railroad Company general mortgage bonds, constituting (with accrued interest) 20.67 percent of the total of the allowed claims of that class voting on the plan, accepted the plan, and that the creditors of that class holding $5,111,100, principal amount, of the bonds, constituting (with accrued interest) 79.33 percent of the total of the allowed claims of that class voting on the plan, rejected the plan.

It is further certified, That the Reconstruction Finance Corporation, sole creditor of class 12(a), holder of The Denver and Rio Grande Western Railroad Company secured notes in the principal amount of $7,581,000 and interest accrued and unpaid as of January 1, 1943, amounting to $2,928,778.31, constituting 100 percent of the total of the allowed claims for that class, accepted the plan.

It is further certified, That the Chase National Bank of the City of New York, sole creditor of class 12(b), holder of The Denver and Rio Grande Western Railroad Company secured note in the principal amount of $1,500,000 and interest accrued and unpaid as of January 1, 1943, amounting to $658,458, constituting 100 percent of the total of the allowed claim for that class, accepted the plan.

It is further certified, That Wilson McCarthy and Henry Savan, as trustees for The Denver and Rio Grande Western Railroad Company, sole stockholder of Class 1, of The Denver and Salt Lake Western Railroad Company, holder of 36,310 shares of the common stock of that company, constituting 100 percent of the total of the allowed claim for that class, accepted the plan.

It is further certified, That the Reconstruction Finance Corporation, sole creditor of class 2, of The Denver and Salt Lake Western Railroad Company holder of a secured note of that company in the principal amount of $3,110,850 and interest accrued and unpaid as of January 1, 1943, amounting to $1,179,976.64, constituting 100 percent of the total of the allowed claim for that class, accepted the plan.

It is further certified, That creditors of class 6, holding $355,500, principal amount, of The Denver & Rio Grande Railroad Company first consolidated bonds, constituting (with accrued interest) 0.88 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) Five ballots, representing $23,000, principal amount, of the bonds, which failed to show whether the ballots were intended for acceptance or rejection of the plan.

[fol. 280] (2) Sixteen ballots for acceptance of the plan (14 of which represented $162,500, principal amount, of the bonds,) which failed to show the serial numbers of the bonds. Two of these ballots also failed to show the principal amount of the bonds.

(3) Ten ballots for acceptance of the plan, representing $30,000, principal amount, of the bonds, which were not supported by documentary evidence of authority to execute the ballots.

(4) Twenty ballots for acceptance of the plan, representing $140,000, principal amount, of the bonds, on which the signatures of the claimants were not witnessed.

It is further certified, That creditors of class 7, holding $138,000, principal amount, of The Rio Grande Western Railway Company first trust mortgage bonds, constituting (with accrued interest) 0.91 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) Thirteen ballots for acceptance of the plan, representing $98,000, principal amount, of the bonds, which were not supported by documentary evidence of authority to execute the ballots.

(2) Five ballots for acceptance of the plan, representing $30,000, principal amount, of the bonds,

on which the signatures of the claimants were not witnessed.

(3) One ballot for acceptance of the plan, representing $10,000, principal amount, of the bonds, which failed to show the serial numbers of the bonds.

It is further certified, That creditors of class 8, holding $38,000, principal amount, of The Rio Grande Western Railway Company first consolidated mortgage bonds, constituting (with accrued interest) 0.25 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) One ballot for rejection of the plan, representing $1,000, principal amount, of the bonds, which failed to show the serial number of the bond.

(2) Five ballots for acceptance of the plan, representing $31,000, principal amount, of the bonds, on which the signature of the claimants were not witnessed.

(3) One ballot for acceptance of the plan, representing $3,000, principal amount, of the bonds, which was not supported by documentary evidence of authority to execute the ballot.

(4) One ballot, representing $3,000, principal amount of the bonds, which failed to show whether the ballot was intended for acceptance or rejection of the——

[fol. 281] *It is further certified*, That creditors of class 10(b), holding $382,000, principal amount, of The Denver and Rio Grande Western Railroad Company refunding and improvement mortgage bonds, series B, constituting (with accrued interest) 3.18 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) One ballot, representing $4,000, principal amount, of the bonds, which failed to show whether the ballot was intended for acceptance or rejection of the plan.

(2) Five ballots for acceptance of the plan, representing $59,000, principal amount, of the bonds, and one ballot for rejection of the plan, representing $4,000, principal amount, of the bonds, which failed to show the serial numbers of the bonds.

(3) Seven ballots for acceptance of the plan, representing $60,000, principal amount, of the bonds, and one ballot for rejection of the plan, representing $5,000, principal amount, of the bonds, on which the signatures of the claimants were not witnessed.

(4) One ballot for acceptance of the plan, representing $35,000, principal amount, of the bonds, and five ballots for rejection of the plan, representing $215,000, principal amount, of the bonds, on which the serial numbers of the bonds were incorrect.

It is further certified, That creditors of class 11, holding $287,200, principal amount, of The Denver and Rio Grande Western Railroad Company general mortgage bonds, constituting (with accrued interest) 0.96 percent of the total of the allowed claims of that class, submitted the following ballots, deemed defective for the reasons stated below and, therefore, not counted with those of other creditors who submitted proper ballots for acceptance or rejection of the plan:

(1) Three ballots, representing $17,000, principal amount, of the bonds, which failed to show whether the ballots were intended for acceptance or rejection of the plan.

(2) One ballot for acceptance of the plan, representing $3,000, principal amount, of the bonds, which was not supported by documentary evidence of authority to execute the ballot.

(3) Three ballots for acceptance of the plan, representing $111,000, principal amount, of the bonds, and four ballots for rejection of the plan, representing $99,700, principal amount, of the bonds, which failed to show the serial numbers of the bonds.

(4) Nine ballots for acceptance of the plan, representing $36,000, principal amount, of the bonds, and two ballots for rejection of the plan, representing $20,500, principal amount, of the bonds, on which the signatures of the claimants were not witnessed.

[fols. 282-283] *And it is further certified*, That the following ballots, more specifically described below, were received or were postmarked after the close of the voting period specified in the order of March 23, 1944, and, therefore, were not counted either with those of creditors who submitted proper ballots for acceptance or rejection of the plan, or with those of creditors whose ballots were deemed defective for the reasons hereinbefore stated:

Class 6. The Denver and Rio Grande Railroad Company first-consolidated bonds

(1) Eighteen ballots for acceptance of the plan, representing $134,000, principal amount, of the bonds, and one ballot for rejection of the plan, representing $10,000, principal amount, of the bonds.

Class 7. The Rio Grande Western Railway Company first trust mortgage bonds

(1) One ballot for acceptance of the plan, representing $5,000, principal amount, of the bonds.

Class 8. The Rio Grande Western Railway Company first consolidated mortgage bonds

(1) Three ballots for acceptance of the plan representing $6,000, principal amount, of the bonds.

Class 10(b). The Denver and Rio Grande Western Railroad, Company refunding and improvement mortgage bonds, series B

(1) Three ballots for acceptance of the plan, representing $150,000, principal amount, of the bonds.

Class 11. The Denver and Rio Grande Western Railroad Company general mortgage bonds

(1) Four ballots for acceptance of the plan, representing $11,000, principal amount of the bonds, and one ballot for rejection of the plan, representing $5,000, principal amount, of the bonds.

the Commission, division 4.

W. P. Bartel, Secretary.

A true copy:

W. P. Bartel, Secretary of the Interstate Commerce Commission. (Seal.)

[File endorsement omitted.]

[fol. 284] IN THE DISTRICT COURT OF THE UNITED STATES WITHIN AND FOR THE DISTRICT OF COLORADO, SITTING AT DENVER

No. 8669

In the Matter of The Denver and Rio Grande Western Railroad Company, Debtor

In Proceedings for Reorganization of a Railroad

HEARING ON CONFIRMATION OF PLAN AND PETITION OF CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE OF THE GENERAL MORTGAGE, FOR CONSTRUCTION OF THE PLAN AND FOR OTHER RELIEF—Filed January 10, 1945

Be it remembered that on, to wit, the 30th day of August, A. D. 1944, the same being one of the regular juridical days of the May Term, A. D. 1944, of said court, this cause came on for hearing before the Honorable J. Foster Symes, Judge of the District Court of the United States for the Judicial District of Colorado.

APPEARANCES:

Henry McAllister, Esq., for the Trustees of the debtor, The Denver and Rio Grande Western Railroad Company.

William V. Hodges, Esq., of the firm of Hodges, Vidal & Goree, for the debtors The Denver and Rio Grande Railroad Company and the Denver and Salt Lake Railroad Company.

Messrs. George D. Gibson, of the firm of Hunton, Williams, Anderson, Gay & Moore, and Morrison Shafroth, of the firm of Grant, Shafroth & Toll, for the Insurance Group Committee.

[fol. 285] Messrs. Edwin S. S. Sunderland of the firm of Davis, Polk, Wardwell, Sunderland & Kiendl, and Robert G. Bosworth of the firm of Pershing, Bosworth, Dick & Dawson for the Guaranty Trust Company of New York, as Trustee.

Messrs. Edward E. Wafts, Jr., of the firm of Mitchell, Capron, Marsh, Angulo & Cooney, and Milton J. Keegan, of the firm of ~~Dines, Dines & Holme~~, for City Bank Farmers Trust Company, as Trustee.

Messrs. James L. Homire and James A. March for the Reconstruction Finance Corporation.

Erskine R. Myer, Esq., for H. Allyn Hicks, Esq., Trustee of the debtor The Denver and Salt Lake Western Railroad Company.

Langdon H. Larwill, Esq., of the firm of Lindsay & Larwill, for the United States Trust Company of New York, as Trustee.

Messrs. William L. Cohn and J. F. Schneider for the Untermeyer Family Group.

Henry H. Larimore, Esq., for Guy A. Thompson, Esq., Trustee of the Missouri Pacific Railroad Company.

Miss Norma L. Comstock for the Central Hanover Bank and Trust Company, as Trustee.

Thereupon the following proceedings were had:

The Court: We have several matters this morning. Can anyone suggest in what order we should take them up? First is the petition of the City Bank Farmers Trust Company as Trustee of the General Mortgage, for construction of the plan and for other relief, and the objection of the debtors, that is, the Denver and Rio Grande—that same objection, and the objections of the City Bank Farmers Trust Company, and the objections of the Missouri Pacific Railroad Company.

Mr. Keegan: If the Court please, the City Bank Farmers Trust Company's petition asks for an adjustment within the framework of the plan as a result of the purchase of the Junction bonds. That particular issue doesn't go to any change or increase in capitalization. It is separate and distinct from the other issues. We have also raised that same point in our objections to the confirmation, asking that this adjustment be made as a matter precedent to the confirmation. We suggest that that narrower issue be heard first. We would like to ask Mr. Thompson a few questions going to that particular issue.

The Court: If there is no objection we will take that matter up first.

Mr. Keegan: If nobody wants to make any further statement I would like to call Mr. Thompson. He is here.

Thereupon the City Bank Farmers Trust Company, to maintain the issues herein on its behalf, offered and gave in evidence as follows:

T. A. Thompson, being called and sworn as a witness on behalf of the City Bank Farmers Trust Company, testified as follows:

Direct examination.

By Mr. Keegan:

Q. Your name is Mr. T. A. Thompson?

A. Yes, sir.

Q. You are the General Auditor for the trustees of The [fol. 287] Denver and Rio Grande Western Railroad Company?

A. I am.

Q. Mr. Thompson, after the Court entered its order last September for the trustees out of cash funds in their hands to purchase the Rio Grande Junction Railway Company First Mortgage bonds, how many of these bonds were purchased by the trustees by December 31, 1943?

A. $1,936,000.00 principal amount.

Q. Will you please state the amount of the cash outlay the trustees used in purchasing the Junction bonds?

A. Approximately $2,750,000.00.

Q. Will you please state the approximate amount of these Junction bonds which have been purchased by the trustees to date?

A. As of July 31st $1,977,000.00.

Q. That is principal?

A. Principal.

By the Court:

Q. What is that difference between that and $2,750,000.00; is that interest?

A. The $2,750,00.00 includes the interest figured on the price of the bonds.

Q. What year?

A. Actually from June 1, 1935—to July 1, 1935—I will get it right after awhile—to September of last year it was—November 1st.

By Mr. Keegan:

Q. Now, of the bonds the trustees have purchased up to July 31st will you state approximately how much they paid

for those, including principal and interest?

A. $2,809,000.00.

Q. This leaves how many Junction bonds still to be purchased?

A. Twenty-three thousand in principal amount for which the price will be approximately $32,679.00.

Q. Will your please state the amount of cash and government bonds that the trustees had on hand January 1, [fol. 288] 1943, the effective date of the plan?

A. $10,850,000.00.

Q. Will you state the amount of cash and government bonds that the trustees had on hand at the date of the hearing on the Commission's plan before this Court last September 16, 1943?

A. $20,000,000.00.

Q. Will you please state the amount of cash and government bonds on hand at the close of last year, December 31, 1943?

A. $20,724,000.00 plus government bonds or cash set aside for deferred maintenance in the amount of $3,751,995.00.

Q. And how much cash and government bonds do you have on hand at the present time, or the nearest date?

A. $17,575,000.00 plus the maintenance fund.

Q. That is plus the $3,751,995.00?

A. That is correct.

Q. Will you please state the amount of the excess of current assets over current liabilities?

A. On January 1, 1943, approximately $7,700,000.00.

Q. Will you please state the amount of the current assets over current liabilities on September 16, 1943?

A. Approximately $12,500,000.00.

Q. On December 31, 1943?

A. $10,400,000.00.

Q. At the present time or at the nearest to the present time you have the figures?

A. As of June 30th $10,850,000.

Q. Mr. Thompson, I hand you some exhibits that have been marked for identification as C. B. F. T. Co. Exhibits Nos. 1 to 8, inclusive. Will you please examine those. Now, Exhibits 1 to 7 are printed Income Account Statements for July, 1943, August, 1943, September, 1943, December, 1943, March, 1944, April, 1944, and July 1944. Exhibit 8

is labeled printed, "Report of The Denver and Rio Grande Western Railroad Company, Wilson McCarthy and Henry Swan, Trustees, Year Ended December 31, 1943." Were [fol. 289] those reports prepared by you or under your supervision?

A. They were.

Mr. Keegan: I would like to offer those in evidence, your Honor.

The Court: They will be admitted if there is no objection.

Mr. Keegan: I have two or three more questions I would like to ask Mr. Thompson.

Q. I call your attention to page 32 of Exhibit 8 which is the 1943 annual report.

Mr. Keegan: Mr. Gibson has asked that on those monthly income account statements, to make the record complete, that we start in with the month of July, 1943, and make it complete every month to date, and we have no objection to that, and if it is agreeable to the Court Mr. Thompson can bring over those other income statements and introduce them a little later. Will that be agreeable?

By the Court:

Q. Are these the regular monthly account statements?

A. Yes, they are.

The Court: Very well.

By Mr. Keegan:

Q. Mr. Thompson, I call your attention to page 32 of Exhibit 8, which is the 1943 annual report. Can the debtor's income available for interest on the funded debt and on that part of the unfunded debt covered by the Reconstruction Finance Corporation loan and the Chase National Bank loan in each year from 1935 to 1943, inclusive, be computed from the figures shown on page 32 of Exhibit 8?

A. They can in short.

[fol. 290] Q. How should those computations be made?

A. Take the first block and take the amount shown as available for interest on funded debt, add into it the columns 2 and 4 covering the RFC loan and the bank loans.

Q. Can the debtor's interest requirements for securities senior to the General Mortgage bonds, including interest on the RFC loan and the Chase National Bank loan for the years from 1935 to 1943, be computed from the figures on this page 32?

A. They can.

Q. How should this computation be made?

A. Well, the shortest method would be to take the $5,208,000.00 and corresponding figures for the previous year in the first column of block 2, add the columns 2 and 4 in block 1 and deduct the $1,490,400.00 shown as General Mortgage interest.

Q. That is column 5 in block 2?

A. Column 6.

Q. Mr. Thompson, I call your attention to Income Account Report for the month of July, 1944, page 2 I believe it is. Does that page show the debtor's income available for interest for the first seven months of this year?

A. It does.

Q. How much?

A. $5,992,836.00.

Q. I call your attention to page 5 in this Exhibit 7. Can the debtor's interest requirement for the securities senior to the General Mortgage for the first seven months of this year be computed from the figures on page 5?

A. They can.

Q. How should that computation be made?

A. Well, the last block of figures on page 5 covers all the interest. Deducting from the $3,411,000.00 the amount of interest shown under "Interest on General Mortgages" of $869,400.00.

Mr. Keegan: Those are all the questions I have of Mr. Thompson.

[fol. 291] Mr. Gibson: May it please the Court, before cross-examination of this witness begins, may it be understood, for I think it would simplify the hearing if it can, that the testimony of this witness will be applicable not only to the City Bank Farmers Trust Company, but also to the confirmation of the plan?

The Court: We will consider it on any question that it is material on. Go ahead with your cross-examination.

Cross-examination.

By Mr. Gibson:

Q. Mr. Thompson, you said that the net available for interest for the first seven months of 1944 was a figure of slightly less than $6,000,000.00. Could you tell us what the corresponding figure was for 1943?

A. $10,286,470.00.

Q. Has that adverse relation of 1944 to 1943 been reversed at the present time?

A. I don't think I understand your question.

Q. Six million dollars were reported as available for interest in the first seven months of 1944 as against $10,000,000.00 in the corresponding months of 1943. That is what I meant by adverse relation. Has that relation been changed since the last report you put in evidence?

A. Well, the figures speak for themselves.

Q. Well, I am asking you to supplement the figures you have put in evidence so far as you can. Are you doing better now than you were in 1943, or worse?

A. Definitely worse.

Q. Does that apply to gross revenues as well as net?

A. Not a substantial degree by any means. The loss in gross for the first seven months is $956,000.00.

[fol. 292] Q. It has been that much less for 1944 as against 1943?

A. That is correct.

Q. Could you give us the figures for the last available period? If that is a weekly period give us the last available week and the last available month, or all the available periods for July.

A. This is through July, Mr. Gibson. We have estimated figures through August 21st of gross only. I don't have those figures with me.

Q. I think it will be sufficient if you will give us the percentage of decline in each of the three periods that are most recently reported.

A. For the period ending August 21st the week shows a decline of 8.79 per cent. The month shows a decline of 5.45 per cent, and the year a decline of 2.74 per cent.

Q. Thank you very much. When you said that from page 32 of the 1943 annual report a calculation could be made of interest on the Chase bank notes and the Reconstruction

Finance Corporation notes I take it you were referring to the stipulated interest on the notes themselves, and not to the collateral. Is that correct?

A. That is correct.

By the Court:

Q. Have you any figures showing the decline in carloadings represented by that loss in gross?

A. Not with me. I can get them on very short notice. I happen to know the decline in carloads was substantially the figure in revenue.

By Mr. Honnire:

Q. Does that decline in loads occur in both government and commercial?

A. Our biggest loss is in bridge traffic which is predominantly government business.

Q. It is due to war operations at this time?

A. Yes sir.

[fol. 293] By the Court:

Q. What is your gross business deficiency?

A. Fifty, fifty-five, probably sixty per cent. I am speaking of bridge traffic.

Q. I mean gross traffic.

A. I wouldn't be surprised if that was fifty per cent.

Q. Would it be that much in gross, government and general business?

A. Approximately thirty-five.

By Mr. Homire:

Q. What is the status of the land grant rates with relation to government business? Is that in a state of controversy?

A. So far as the Rio Grande is concerned there is no direct controversy. We are seriously involved as an intermediate carrier, and the settlements are made in our case by the terminal lines and the majority of it by the western lines. Therefore we are unable to do anything but guess as to the amount that could be involved in those disputes.

Q. Should those disputes result in an adverse decision to the railroads, what effect would that have on the cash position of the Rio Grande?

A. It would mean we would have in effect to give back cash or reduce our current remittances in the amount of the land grant deductions.

Q. They might be very considerable if that question was resolved against the railroads?

A. They could be substantial.

By the Court:

Q. In these cash balances, have you taken into consideration the deductions allowed for income taxes?

A. The bonds include bonds purchased to pay income taxes.

Q. Have you paid all your income taxes up to date?

[fol. 294] A. Federal income.

Q. Would that be the figures you have given? Would the balance of the cash available be affected?

A. There is approximately $3,500,000.00 in taxes due at this time. That is for the balance of this year plus the current year's accumulation.

Q. You haven't deducted that from the balance you have given?

A. We have not.

By Mr. Keegan:

Q. In other words, in your excess of current assets over current liabilities, it is in there and not taken out?

A. Yes.

Mr. Gibson: There is one question I overlooked, if your Honor please.

By Mr. Gibson:

Q. In the annual report to stockholders for 1943 that you introduced in evidence, Mr. Thompson, at page 5 a summary is given of the increases in wages to employees, and that discussion concludes with the statement about the middle of page 5: "It is estimated, on basis of present force, that the increases now in effect"—those are increases in wages—"on an annual basis, will amount to $2,700,000." I would like to ask whether that statement is still substantially representative of the existing situation?

A. I believe it is accurate as any we could make even to date.

By the Court:

Q. Does that mean that much additional will have to be paid out on the cash basis?

A. No, that would mean the normal pay roll costs 1944 over 1943 prior to the wage increases. 1943 expenses include in them as much of the retroactive pay as we could possibly see at the time we closed the report.

[fol. 295] By Mr. Hodges:

Q. Mr. Thompson, you have testified that there has been paid out approximately $2,800,000.00 to take up the Junction bonds?

A. Correct.

Q. And you have given us the figure for the amount that was paid in the year 1943. Did you consider the charging of that amount to the operating expenses of the gross operation?

A. No. We are carrying it in the trustees' investment account.

Q. You didn't so charge it?

A. I did not.

Q. And you have also paid out a considerable sum in this year, 1944, for the acquisition of further amounts of those bonds, and that has not been charged as a part of the operating expenses of the gross proceeds?

A. That is correct.

Q. Now, Mr. Thompson, have you with you the data showing the analysis of the traffic of this road on which you base an estimate of thirty-five per cent government business?

A. I don't have it with me. I happen to know that our government business amounts to 10,000 to 12,000 carloads a month out of a total——

Mr. Homire: The witness testified fifty per cent rather than thirty-five per cent.

The Witness: My last figure was thirty-five per cent of all traffic.

By Mr. Homire:

Q. Fifty per cent of bridge traffic?

A. That is right.

(Last question and answer read.)

A. (Continuing:) Out of a total of approximately thirty thousand cars per month.

[fol. 296] By Mr. Hodges:

Q. That data from which you deduced that statement is available, is it not?

A. It is available, but I don't like to put it in the record.

Q. I wouldn't think you would. I would like to take time to see it, and maybe recall you, but I would like to see it and go over it with you, and see on what factual basis your opinion is based.

A. All right.

Mr. Hodges: Of course, I call the attention of the Court to the fact that the factual basis should be here as distinguished from his opinion.

Q. I hold here, Mr. Thompson, the published balance sheet of December 31, 1943, and I am looking at current assets and current liabilities. Have there been any adjustments made in the figures shown on that report since the report was authenticated and issued?

A. Nothing in the way of adjustments, but we make our balance sheet monthly of course, and file it with the Court.

Q. I don't believe my question is clear to you. In looking at your reports for 1942 as of December 31st, and then looking at the recapitulation of that report or the restatement of those figures in your report of December 31, 1943, I find that there are some differences in figures, and I assume that even after you made your annual report you had to make some adjustments. Do you recognize that any adjustments were made in the report of 1942, for the year ending December 31, 1942?

A. Offhand I do not recognize any.

Q. Well, you are certain, then, that we can take the report of December 31, 1943, as a correct report, and not subject to adjustments for the period represented by that report?

[fol. 297] A. I think you can.

Q. In fairness to you and to myself if I have made a mistake about adjustments in 1942, I will take time afterwards to look at that again. I thought I saw some substantial adjustments, and I may be mistaken. Now, did the accident

in the tunnel on the Salt Lake line affect your business for 1943?

A. Substantially, yes.

Q. When was that traffic resumed?

A. On December 1, 1943.

Q. So it has not affected your 1944 traffic, or are you prepared to say whether it has or not?

A. Well, I can only say to the extent that diversions made against us during that period may have been partially continued. I don't know.

Q. That was an interruption in the ordinary relationships with the patrons of the road?

A. Substantially.

Q. And, as a matter of fact, it involved a considerable loss in 1943, did it not?

A. It materially affected our operating results for 1943.

Q. Have you ever actually figured out what loss that represented in the year 1943?

A. It can't be figured.

Q. That is one of the things that can't be figured?

A. It can be guessed at, but that is all.

Q. Well, can you figure any more definitely what part of your traffic is government traffic and what is not?

A. No.

Q. That is an estimate, isn't it?

A. That is still an estimate.

Q. Who would do the figuring to determine how much damage was done to the business of this railroad of 1943 [fol. 298] by that tunnel accident?

A. I think we should all take a shot at it.

Q. And, as a matter of fact, all of you who have special knowledge concerning the effect have talked together and considered it and arrived at an approximate estimate, have you not?

A. Well, we did talk about an estimate before the tunnel was even opened, and it continued out of service for a longer period than that, and all we can do now is just to make an approximation of revenue which was lost.

Q. What you did then is to make an approximation?

A. Yes, that is right.

Q. And you can make an approximation now?

A. Yes, on the basis of diversion orders out against us.

Q. When did you begin to pay federal income and excess profits taxes?

A. We have never paid any excess profit taxes. We paid federal income in 1942.

Q. That is the first year?

A. That is the first year.

Q. Up to that time you had not paid the government anything on account of the federal income tax. Now, in 1942 how much income tax did you pay the government, the federal government? I ask you that because while I see the item of taxes paid in your annual report, I can't be sure that I can tell what was federal income tax.

A. In 1942 our accruals, which were approximately our payments, were $2,180,000.00, of which $1,700,000.00 approximately was federal income taxes.

Q. That is an accrual figure for 1942?

A. That is correct.

Q. You would have definite data, wouldn't you, as to the amount actually paid for the 1942 income taxes?

[fol. 299] A. I have the figure, yes.

Q. Well, you have said it is approximately that amount.

A. Naturally the accounts have to be closed on the accrual basis and closed long before the tax is actually figured out.

Q. I am not asking you, though, what the accrual was. I am asking what the payment was. I have seen accruals made in perfect good faith which didn't turn out to be the actual taxes paid during that year. That can be so?

A. That can be so, yes.

Q. But in your particular case you are prepared to say you accrued it with accuracy within a very few dollars one way or the other?

A. They were fairly close.

Q. And you think that in 1942 you paid $1,700,000.00 to the government for federal income taxes?

A. That is approximately the figure. The figure was somewhere between $1,600,000.00 and $1,700,000.00.

Q. At least, then, can we settle on this: that it didn't exceed $1,700,000.00?

A. That is correct.

Q. And it was not less than $1,600,000.00?

A. That is correct.

Q. Well, that is close enough for me. And if that wasn't a proper charge against the operating expenses of the debtor's trustees, your showing of net income for that year would be increased accordingly?

A. That is correct.

Q. What income tax did you pay in 1943?

A. For 1943?

Q. Yes.

A. Our return has not yet been filed. We are paying on an estimated basis of a total tax of $6,800,000.00 federal income taxes.

Q. Now, in 1943 I see accrued tax liability of $9,186,-
[fol. 300] 723.32. That is in your report of December 31st?

A. Correct.

Q. And if approximately $6,000,000.00 of that was federal income tax——

A. $6,800,000.00.

Q. $6,800,000.00?

A. That is right.

Q. That would leave something like two million three or between two million three and two million two for other taxes. What else is included in that two million?

A. Income taxes to the State of Colorado and to the State of Utah and our general ad valorem taxes.

Q. How much of that was income tax to the State of Colorado?

A. About $220,000.00.

Q. And how much was income tax to the State of Utah?

A. Approximately $150,000.00.

Q. That is about $370,000.00 more income tax than that payable to the federal government?

A. That is right.

Q. You had that same situation in 1942, did you not?

A. We did.

Q. What was your state income tax in 1942, Colorado, then Utah?

A. As I recall that, it was $200,000.00.

Q. And Utah?

A. Utah about $90,000.00.

Q. Now, while that is your accrual of income taxes, you have not paid all of that yet, have you?

A. We have paid half of Colorado, half of the federal, and none of Utah.

Q. And that payment of federal and Colorado tax that you are now speaking of is applicable to the year 1943?

A. That is correct.

Q. How near to your accrual is that actual tax?

A. For 1943?

Q. For 1943, or do you know yet?

[fol. 301] A. The total is within $10,000.00 of our accruals.

Q. So that we can take that accrual as being remarkably close to the actual tax?

A. That we are going to pay.

Q. That you are going to pay. If that tax is not a proper expense of the trustees in their operation of this property, then your 1943 income, net income, would be increased quite substantially, would it not?

Mr. Gibson: We object to that question on the ground that a purely hypothetical question has been asked if the federal government income taxes were not proper expenses. The contingency is so remote.

Mr. Hodges: My dear sir, the contingency is right on your neck right now.

The Court: Answer that yes or no.

A. Yes.

Q. And can you state the amount by which it would be so increased?

A. About $6,800,000.00 as applicable to federal. I don't know that your question included the state.

Q. I will, if I didn't include the state in the question—I will now include that.

A. Then it would increase it by the amount of accrual shown, $7,184,000.00.

Q. Now, for the income tax accruals what is the difference between the 1942 and the 1943 net income?

A. It gives a net income for both years of approximately $13,000,000.00.

Q. Now, you have accrued some income taxes for the year 1944, have you not, in the statement you have given us?

A. We have.

Q. I have not seen that. Is that all in one exhibit?

A. That is in the exhibit that has been introduced in evidence.

[fol. 302] Q. May I see a copy of that exhibit? I don't know which one it is. I will identify it in a moment. Let's see what exhibit that is.

A. Exhibit 7.

Q. Have you an extra copy of it there?

A. I have my own copy.

Q. Well, just keep it then. I will use the court copy. Now, we are talking about the accrual of income taxes, fed-

eral and state; for the period January 1 to July 31, 1944 I see it, Mr. Thompson. Railway tax accruals.

A. It gives the details in the first block on page 5.

Q. Well, I get it for the month of July, 1944, in the first column on page 5, but it is in the fifth column of the first block; is that correct?

A. That is correct.

Q. And there is an accrual of $1,675,700.00 for federal and state income taxes for the first six months of 1944?

A. For the first seven months.

Q. Or a reduction of 65.16 per cent over the same period in 1943?

A. That is correct.

Q. Now, in computing your accrual you are computing a very much lower income for 1944 than you had in 1943; is that correct?

A. That is correct.

Q. Now, in this same exhibit there is a statement of operating revenues for the same period, and I find that on page 2, and I find that there is in the last column in the first block on page 2—that there is a reduction in operating revenues of 2.38?

A. That is correct.

Q. And that the freight revenues have fallen off 3.45?

A. That is correct.

Q. Now, in the next block of operating expenses am I correct that in this period there has been an increase of [fol. 303] 54.76 per cent in maintenance of way and structures, roadway and track?

A. No, the total is 59.43 per cent.

Q. Well, now, I look at this and I read 54.76.

A. That is breakdown of the roadway and track structure alone.

Q. That is what I said.

A. Well, the bridges are a part of that too, but they are separate.

Q. That is set up in a separate block, isn't it?

A. That is correct.

Q. Bridge structures increase of 53.3?

A. That is right.

Q. Now, how do the actual expenditures for maintenance of way and structures conform to the expenditures in 1943?

A. That would require considerable analysis. Without an analysis I can't answer your question.

Q. There is someone in the organization who would have that, is there not, or would that be in your office?

A. These are the figures in our office or almost any office.

Q. Any office that had the figures?

A. That is right.

Q. Reliable as they are in your office. I will go into that a little later because that raises this question. In computing your income for 1942 did you deduct more than the normal maintenance expense?

A. 1942?

Q. Yes.

Mr. Homire: I think that is an objectionable question. We object to it because we don't know what the "normal maintenance" means.

The Court: Objection overruled. You can clear it up on cross examination.

A. I don't know of any extraordinary charges in 1942 to maintenance other than some minor charges to amortization.

Q. Well, I think we can get at it more simply by ourselves [fol. 304] taking your reports here and comparing maintenance expense for several years, without asking you specifically about this, and it will shorten it very much. Now, in arriving at your net income I see where there appears in 1942 an item "Accrued depreciation road and equipment"?

A. That is right.

Q. When was that account first introduced?

A. The figures that are used in 1942 have been in effect since 1910.

Q. Since 1910?

A. 1910 through 1942 on substantially the same basis.

Q. And this road has accrued a depreciation on equipment?

A. Equipment only.

Q. So that there really in the figures shown in 1942, $15,351,301.89 really is equipment depreciation?

A. That is correct.

Q. In these former years did you use the designation "Road and equipment," or just "Equipment"?

A. That is ICC designation—"Road and equipment." That is, depreciation of road property was optional until January 1, 1943, when it became mandatory.

Q. That is, the Commission made a ruling to that effect?

A. That is correct.

Q. And you are now following that ruling in 1943?

A. That is correct.

Q. And you have in that item in 1943 of $16,870,152.00—you have a factor which represents road depreciation as distinguished from equipment?

A. That is correct.

Q. Approximately how much is that?

A. Approximately $700,000.00.

Q. Was that determined from inspection of the depreciated property?

A. No, that is using the 1C'C formula.

[fol. 305] Q. Straight line formula?

A. That is correct.

Q. And not based upon inspection of the evidence?

A. That is correct.

Q. Now, here is another item, "Accrued amortization of defense projects equipment." When did that first come into the accounts?

A. I believe the amortization regulation came into effect January 1, 1942.

Q. So that you have an item of $743,281.78 deducted from the income of that year which you call accrued amortization of defense projects?

A. That is correct.

Q. Was that all on equipment?

A. In 1943 or 1942?

Q. 1942.

A. 1942 ninety-nine per cent of it was on equipment; a very small amount to road.

Q. Was that in addition to your equipment depreciation, the figure on the——

A. It was not. You mean used for both?

Q. But you did have in that year accrued depreciation on equipment of close to $14,750,000.00?

A. That is the accumulated figure from the date the depreciation started. The charges for the year are in the report.

Q. So that this item of amortization of defense projects is your total equipment depreciation which you deducted from earnings for that year?

A. When you speak of amortization you use your figure for depreciation.

Q. Well, let me reframe that question. You do, in arriving at your net income for that year, deduct an amortization of defense projects, do you not?

A. We do.

Q. And that applies to equipment?

A. That applies to equipment.

Q. And that is the figure shown in your 1942 report as [fol. 306] accrued amortization of defense projects?

A. Not necessarily. I say the accrued figure in the balance sheet is an accumulated figure.

Q. But it is the same figure in the income account, isn't it, for that year, because that is the first year you used it?

A. That is correct.

Q. So we are just at the same place where we split off?

A. As to 1942 we are.

Q. Yes, as to 1942. Now you come to 1943. Just indicate the page where I will find those deductions from your income account.

A. Find them on pages 16 and 17, accounts 270½ and 331½.

Q. Now, for 1943 in the account 270½—no, that is not the same thing, is it?

A. That is amortization of defense projects.

Q. That is not equipment?

A. Equipment is under 331½.

Q. All right. Now I have got it. Your equipment amortization of defense projects, $1,173,007.37, is deducted in arriving at your net income for the year?

A. It is.

Q. Is that all the deduction taken by way of amortization, obsolescence or depreciation of equipment?

A. No, shown in account 331 is normal depreciation.

Q. That is not charged to your normal depreciation?

A. That is correct, except that it is the same thing, because when we take amortization we don't take normal depreciation.

Q. On the same items. But you take normal depreciation on the others. Is that based on inspection?

A. It doesn't require inspection. We have certificates of necessity that authorize it under the section of the income [fol. 307] tax law over a period of sixty months or less if the war should end, for the purpose of income tax savings.

Q. But it is not an engineering amortizable figure?

A. That is correct.

Q. It just says you may take a certain percentage of items and amortize them as war instrumentalities?

A. That is correct.

Q. So that when this went in under that law you charged up against income this amortization factor which the law lets you do, but it represents no engineering fact; is that correct?

A. That is correct.

Q. All right. How about road structures?

A. Amortization there.

Q. Amortization there.

A. Amortization of road could involve property that is not depreciable as well as depreciable property.

Q. What account is that?

A. 270½.

Q. That is the one I lighted on first, wasn't it?

A. Yes.

Q. Well, what was the amount of amortization of road structure that was deducted in the year 1943? I have got it here. It is a trifling item, approximately $45,000.00.

A. Approximately $45,000.00.

Q. How about your account 268 where there is a deduction in this year for deferred maintenance of $1,586,577.00; is that correct?

A. That is correct.

Q. And that is in addition to your actual maintenance expenditures for that year?

A. That is correct.

Q. And that gives you some kind of a credit, does it not?

A. Sets up a reserve to take care of maintenance that was [fol. 308] not done in 1943.

Q. Have you set aside cash to take care of that reserve?

A. Cash or bonds, yes.

Q. And does that cash appear in your statement of cash on hand?

A. It does not.

Q. So that when you testified that you had certain cash on hand I think you stated it correctly there, that when you state your cash on hand, you leave out an amount of cash that is set aside to make this deferred maintenance reserve?

A. That is right.

Q. And did you state the amount of that cash?

A. I did.

Q. At the present time it is my understanding that exceeds $3,000,000.00. I just want to refresh my recollection.

A. It is in excess of $3,000,000.00, yes sir. I might say that some $400,000.00 of it has been expended this year, and the credit of that expenditure is reflected in the figures for 1944.

Q. You mean by that that $400,000.00 will not come in as an expense for the year 1944?

A. Not in our ICC or printed income accounts or reports to the Commission.

Q. So that in future years as you do maintenance and desire to charge some of it to this account—should I say charge or credit?

A. We charge that to the account.

Q. Charge some of it to that account, by that much you improve the earning picture for the year?

A. That is right.

Q. For the year 1943 under the law you deduct that reserve before computing your net income?

A. For ICC and other purposes, but not for income tax purposes.

Q. So if you have income taxes to pay you have to pay on [fol. 309] that?

A. That is definitely correct.

Q. And that has been included in your computations for income taxes for the year 1943?

A. Yes.

Q. You can make no charge other than for income tax purposes?

A. Not at the present time.

Q. And yet in the showing in your report as to the net income for the year 1943 there is $1,500,000.00 deducted and set aside in that reserve?

A. $3,500,000.00.

Q. For one year?

A. For the year 1943, yes sir.

Q. That is worse than I thought it was. I picked up a figure of $1,500,000.00 here in your——

A. You took the maintenance of way only.

Q. Oh yes, I took the maintenance of way.

A. Our figure includes equipment as well.

Q. And is there a cash reserve set aside for that equipment too?

A. There is.

Q. Not included in your cash on hand?

A. That is right.

Q. As I look now, Mr. Thompson, at your Exhibit 7 I see that for these first seven months of the year 1944 you have approximately $800,000.00 less gross revenue. Note I use the word "approximately."

A. The estimate was $956,000.00.

Q. Are you looking at No. 7?

A. Yes.

Q. I was looking at the month of July rather than the period of seven months. We will call it roughly $1,000,000.00 less income.

A. That is right.

Q. Now, you have got operating expenses have increased $4,817,736.72 or 21.63 per cent.

A. That is what the report shows.

Q. There is a large increase in 1944 in maintenance of way and structures of approximately $2,000,000.00.

[fol. 310] A. I will call it $1,900,000.00.

Q. And is that in addition to the $400,000.00 that has been charged to reserve?

A. That is in addition to the $273,000.00 charged to the maintenance of way part of the reserve.

Q. And the remainder of that $400,000.00 has been charged since this period?

A. Yes.

Q. Or when you used the figure of $400,000.00 did you include maintenance of way and equipment?

A. And maintenance of equipment.

Q. Now, I notice that the maintenance of equipment has increased by $1,703,000.00. I will agree with you and call it $1,704,000.00.

A. All right.

Q. Or 26.91 per cent.

A. That is correct.

Q. And that is in addition to what has been charged to maintenance of equipment reserve fund?

A. That is right.

Q. Is a large part of that additional expense there reflected in higher wages for employees?

A. Very substantial. The wage increase in effect today is approximately twenty-five per cent over the wages that are reflected in the figures of last July. That naturally picked up in November and December of 1943. We couldn't make them up in July. Therefore the comparable figure of last year includes a wage increase of approximately twenty-five per cent.

Q. Well, does that include payment for wages performed in 1943 that are paid in 1944?

A. There are no 1943 wage costs in 1944, that is, no substantial. Naturally we had to make an estimate for 1943, but we were within $50,000.00 or $60,000.00.

Q. Your transportation costs have gone up $953,000.00 plus?

A. That is right.

[fol. 311] Q. We will say $953,000.00. Is that largely due to wage increases?

A. Practically all of it.

Q. You gave us some figures as to the cash on hand on July 31st or August 31st.

A. June 30th was the last.

Q. June?

A. Yes, sir, that was the last published balance sheet.

Q. Was there one published at that time? Did you put it in evidence here?

A. Not today. It has been filed in court.

Q. Have you got more than one copy there?

A. I have the balance sheet. There is only one copy.

Q. Well, maybe we can get at it without my looking at it if I can find the balance sheet in here. Will you look at your last balance sheet? Now, what cash did you say you had on hand according to that balance sheet?

A. Actual cash is $6,570,000.00.

Q. And what temporary cash investments?

A. $11,005,000.00.

Q. What special deposits?

A. $2,900,000.00.

Q. Are those deposited and earmarked against something?

A. Special deposits are definitely earmarked.

Q. What are they earmarked for?

A. A lot of things.

Q. Well, now, let me put it another way to save you trouble. Any of those earmarked for your reserve fund?

A. No, sir, they are not. That is in a special account, "Maintenance Fund," not included in those figures I gave you.

Q. How about this general question: Was the $2,000,000.00 of special deposits earmarked to pay some of the current liabilities that are in your balance sheet?

A. Well, the biggest part of them on this balance sheet is the $2,700,000.00 of interest to be paid on July 10th, the [fol. 312] amount deposited with the various paying agents to pay the 1943 interest.

Q. That was the interest——

A. A big part of that $2,900,000.00 is that interest money.

Q. Well, on July 31, 1944, what were your total current assets?

A. They have not been published yet.

Q. Is it not on your report there?

A. June 30th.

Q. It would be much easier if you would say "Mr. Hodges, I have it for June 30th." I am not trying to trap you to get some information. Give it to me for June.

A. 33,285,000.00.

Q. And what are current liabilities?

A. $22,430,800.00.

Q. And the difference between your current liabilities and your current assets on that date are in substance different than the difference between your current liabilities and current assets on December 31, 1943?

A. They are very, very close together.

Q. Meantime you have paid out the Junction interest of about $2,700,000.00?

A. That is right.

Q. Now, have you some inside information as to how things stand today as distinguished from June 30th?

A. I do not.

Q. [illegible]w what your cash balance is today?

A. [illegible] sir.

Q. It is not as good as it was June 30th, is it?

A. No.

Q. Well, let's have it.

A. The balance as of August 28th $6,183,000.00.

Q. Have your temporary cash investments increased?

A. No, they have not.

Q. Any special deposits? As a matter of fact, they have [fol. 313] decreased?

A. The special deposits naturally decrease on the payment of interest.

Q. Unless you get some more. Have the trustees any special accounts or reserves in which the cash is deposited not included in these statements?

A. Other than definitely earmarked deposits, but they are all included in these statements.

Q. The three million and one-half reserve is not included in your cash statement?

A. That is correct. I have said that is a special account called "Maintenance Fund."

Q. Now, have you any other reserves where there is cash to take care of them that do not appear in your cash?

A. No other than earmarked for special things.

Q. That is what I want to know.

A. I can read into the record the detail of these special deposits if you wish. There are no others.

Q. It is not so much I want the detail, but I think I can frame a question that you can answer very easily without being trapped. You have here one reserve of $3,500,000.00, and you have set aside and earmarked some money to take care of it, and it doesn't show in your cash account?

A. That is correct.

Q. Is there another reserve where the cash has been set aside and it doesn't show in your cash account?

A. I don't know of any.

Q. Is there any other special account where there is cash that does not show in your cash account?

A. Not that I know of.

Mr. Hodges: Thank you. Mr. Thompson, I may want to call you back on some of these things after I have a [fol. 314] chance to look at these records and see if there is anything I want to verify.

Mr. Shafroth: If the Court please, we discovered this morning that we had neglected to file the answer of the Insurance Group Committee. It was discussed in New York in June, and a copy was supplied to Mr. Watts at that time. A copy of this answer—through inadvertence it was not filed. We ask permission to file it at this time.

T. A. Thompson resumed the stand for further

Cross-examination.

By Mr. Homire:

Q. Mr. Thompson, you referred to the tunnel accident that occurred last year. Will you state for the record what that accident was?

A. We had a fire and cave-in in tunnel No. 10 of the Moffat Tunnel road on the Denver & Salt Lake Railway which occurred on September 20th and was opened on December 1st, necessitating rerouting of all traffic by the Royal Gorge route.

Q. You have testified to a decline of the gross earnings of the railway, gross revenues, which is in comparison with the decline in the net rather slight. Can you give me the reasons in general for the great decline in net as compared with the rather smaller decline in gross?

A. Well, there is the increased charges to amortization, and the major cost, of course, being the increased cost for both labor and material.

Q. Have you made any studies or study as to the comparison of present unit costs of materials and supplies with any earlier period?

A. I made a study some two or three months ago; com- [fol. 315] paring with the costs of 1939.

Q. Comparing current unit costs with unit costs of 1939?

A. Yes, both labor and material.

Q. Will you state the result of your studies and percentages on both materials, supplies and labor?

A. That study showed an increase of approximately sixteen percent in the unit cost of materials and supplies, and an increase of between twenty-nine and thirty percent in the basic hourly rates for all labor.

Q. Have you any results of that study in terms of dollars that you could give us at this time?

A. I haven't. I could calculate it very easily from the information I have in my office.

Q. If we continue after lunch would you produce that at that time?

A. I will be glad to.

Q. What is the present annual accrual for roadway depreciation of the railroad?

A. Approximately $790,000.00.

Q. And does that include shop machinery that is used in the repair and maintenance of equipment?

A. It does.

Q. You testified that the Commission changed the accounting rules pertinent to depreciation of roadway and structures, making that depreciation mandatory instead of optional, and that that change took effect I believe January 1, 1942?

A. January 1, 1943.

Q. 1943. Will you state your understanding as to why the Commission made that change?

A. I presume because they thought it was sound accounting. The Commission has since 1925 had a docket of its own, endeavoring to set up depreciation on road accounts, and it has been discussed back and forth between the various railroads and the AAR, and finally in 1942 they issued [fol. 316] an order making it mandatory as of January 1, 1943. Prior to that time it was optional, and I believe utilized by very, very few railroads.

Q. And it would be presumably the purpose of sounder accounting practice for the purpose of reflecting more accurately the available income?

A. I think so.

By Mr. Gibson:

Q. You said accruals for roadway depreciation approximated $700,000.00. I was wondering if we could be slightly more exact. I notice on page 4 of the 1943 annual report to stockholders a statement that the accruals for roadway depreciation were $664,000.00 chargeable to maintenance of way and structures, and $112,000.00 to shop and power plant machinery which is charged to maintenance of equipment expenses. The total of those would be about $775,000.00 or $776,000.00. Would that be a more accurate figure?

A. That would be a more accurate figure.

Mr. Homire: Thank you.

By Mr. Hodges:

Q. Mr. Thompson, you have given your opinion on this accounting question in the deduction of depreciation on road and structures. You know that the railroads resisted it for a great many years?

A. I do that.

Q. And did you know the legal reasons for resisting it?

A. Not without going back and looking them up.

Q. You didn't take into consideration in giving your opinion the rulings of the Supreme Court of the United States on the question of depreciation?

A. I did not.

Q. You know that this depreciation is not based on inspection?

A. That is right.

[fol. 317] Q. And you know that the attitude of the railroads over all these years has been that there is no such depreciation?

A. I am familiar with that.

Q. And that for all these years the Interstate Commerce Commission has merely said to you "Well, take it if you want to"?

A. That is correct.

Q. And now they have made a ruling, and do you have any information on whether that ruling is good as against the law as declared by the Supreme Court?

A. Not from a legal standpoint.

Q. Now, you said that there is an increase over 1939 of sixteen per cent in material cost?

A. That is right.

Q. How wide a field do you cover in that material?

A. Approximately ninety per cent of all material used.

Q. Rails?

A. Rails.

Q. Ties?

A. Ties, coal.

Q. Everything that goes into the construction of a railroad?

A. Maintenance in particular.

Q. Maintenance is really keeping up the constructive plan, isn't it?

A. Yes sir.

Q. You say that is sixteen per cent?

A. Sixteen per cent, yes sir.

Q. And you say that the labor costs have gone up about 29%?

A. That is right, twenty-nine to thirty per cent.

Q. That is not your own opinion, is it?

A. Well, for the record I will state that I made a very careful study and comparison of the present day costs with 1939 costs. The wage rates are a matter of record in the reports of the Commission. I used those reports, and, incidentally, thirty days after I made that report the Interstate [fol. 318] Commerce Commission made a study for the railroads of the United States and quoted the identical figure on wage rates in the nation-wide area.

Q. Well, so far, then, as material and unit costs enter into the estimate of the reproduction cost of the railroad, you would have to increase your material costs by about sixteen per cent and your wage costs by twenty-nine to thirty per cent compared with estimates made in 1939?

Mr. Gibson: I think that is purely a legal question. Any gentleman can answer that quite as effectively by briefs as they can by the witness on the stand.

The Court: I wouldn't ask anything about a Supreme Court decision. I would just ask him what his figures show.

Mr. Hodges: It is not asking what the Court said. Before I did ask him that, and he so testified, because he gave an opinion as to a certain account, and I didn't object to it. This is a factual thing.

Q. (Question read to the witness.)

A. Yes.

By Mr. Gibson:

Q. But even after doing that, you wouldn't earn any more, would you?

A. No.

The Court: Is that all of this witness, gentlemen? Step down.

Mr. Keegan: If the Court please, the City Bank Farmers Trust Company has about three more exhibits here. We probably will have——

Mr. Gibson: May it be understood that this forthcoming evidence will be applicable to all the issues raised herein?

[fol. 319] The Court: Yes.

Mr. Keegan: We have an exhibit here marked 9 and they want another letter to go with it. I would like to reserve that until after lunch, and go ahead with the exhibits that have been marked for identification as Nos. 10 and 11. If the Court please, in explanation of our Exhibit No. 10 you will recall that Mr. Thompson on our direct examination stated that if we wanted to compute the debtor's income available for interest so as to include the Reconstruction Finance Corporation's interest and the Chase National Bank loan interest you would take columns 2, 4 and 6 in the top block of figures on page 32 of the 1943 annual report, Exhibit No. 8, and add those three columns together. That is what we have done on the computation for column II of

Exhibit 10. Mr. Thompson stated that would be the way to make it. In the third column of Exhibit 10 under the heading "Debtor's Interest Requirements for Securities Senior to General Mortgage Bonds including Interest on Unfunded Debt," there again we have simply made the computation which Mr. Thompson said should be made, namely, adding the total interest on the funded debt as shown in column 1 of the second block of figures on page 32, and added to it the RFC and the Chase National Bank loan interest and then deducted the $1,494,400.00 interest on the General Mortgage bonds in order to get the senior interest ahead of us. Then, the last column IV of Exhibit 10 is simply the difference between columns II and III. It shows each year whether the debtor's income available for interest was more or less than enough to take care of the interest on senior debts ahead of us. The summaries are given and the only one that is estimated—the only figure that is estimated is [fol. 320] the income for the balance of 1944. We have the exact figures for the first seven months, and we have estimated that it would keep up at that same ratio, which I think is ultraconservative, and we figured the entire income of 1944 on that ratio. I had these figures added and subtractions made by our bookkeeper and checked by our office auditor, and then I checked the adding machine tape, and to the best of my knowledge they are accurate.

Exhibit No. 11 simply starts out with the first plan of reorganization which was submitted, which was the debtor's plan back in 1936; shows what the proposal was; how much stock in the reorganized company it was supposed to give the General Mortgage bonds at that time; what the current earnings were at the time that plan came out, and what the accumulated earnings over senior interest to last December 31st were at that time. We have given in a footnote there a reference to the printed record where all of those plans can be found, and the amounts in column III as to what the proposal was to give the General Mortgage bonds in each plan throughout the years, that was taken from the part of the record indicated in the footnote. Then we come to column IV to find out what the current earnings were for that particular year when that plan was proposed. Those figures are simply transposed from our Exhibit 10, and the accumulated surplus is also transposed from our Exhibit 10. It is just a matter of running them off on the adding ma-

chine. I would like to offer at this time our City Bank Farmers Trust Company's Exhibits Nos. 10 and 11.

The Court: Is there any objection? If not, they will be admitted.

Mr. Homire: Is there to be no witness introduced to support these?

[fol. 321] Mr. Keegan: I am perfectly willing to swear, if you think it is necessary, that these computations—we had Mr. Thompson testify how the computations should be made. The question of computations was just running them off on the adding machine and making the necessary additions and subtractions.

Mr. Homire: I would just like to ask you one or two questions. In the exhibit that shows the various balances made on various plans, what number is that?

Mr. Keegan: That is No. 11.

Mr. Homire: Of course, the capitalizations that are subjected to your analysis here in the various plans were not always the same in the various plans: is that not true?

Mr. Keegan: That is correct. You mean, for instance, the debtor's plan in 1936 would have one capitalization, and the Insurance Group plan No. 1 would have another capitalization?

Mr. Homire: Yes.

Mr. Keegan: That is right.

Mr. Homire: So the capitalizations vary, and taking a percentage of allotment to the General Mortgage under one capitalization would not necessarily be an exact or intelligible comparison with another percentage under another capitalization. That necessarily follows from the fact that the capitalization was different.

Mr. Keegan: I would suggest you put in the capitalization, and you can draw your own conclusions. We had that as an exhibit in one of our briefs.

Mr. Homire: I don't think it is necessary so long as you say the capitalization under the different plans is different. [fol. 322] Mr. Keegan: This is not a per cent of the capitalization. For instance, take line 1 of Exhibit 11, and under III we note the debtor's original plan or proposal was to give the General Mortgage bonds new stock equal in par value to 100 per cent of their claim, and so on down the line.

Mr. Homire: But you are giving them fractions of the different capitalizations in the different cases you compared.

Mr. Keegan: The capitalizations vary. I will be glad to give you the proposed capitalizations if you think that will help.

Mr. Homire: I don't think it is necessary. I just wanted to bring out the point the capitalizations were different. The only other objection is that during the progress of the proceedings the senior debt was increasing on account of the accumulated unpaid interest. That also is a fact, is it not?

Mr. Keegan: That is a fact. That is shown graphically on this Exhibit No. 10. It shows it year by year down to the date of the plan.

Mr. Hodges: I should like to put in a caveat to that statement.

Mr. Gibson: Will you let me ask a question or two for information there?

Mr. Keegan: Certainly.

Mr. Gibson: Is the purpose of these statements to support a request by the General Mortgage bondholders for a payment of cash to the General Mortgage bondholders, or for some increase of securities to the General Mortgage [fol. 323] bondholders?

Mr. Watts: May I answer that question? Mr. Keegan prepared these exhibits at the request of the General Mortgage Trustee and its New York counsel. They are to be used just incidentally in connection with Mr. Keegan's question of the possible redistribution of the bonds of the reorganized debtor which were released through the purchase of the Junction bonds, but primarily and principally they are to be used in connection with the question of the reasonableness of the action of the General Mortgage bondholders in voting to reject the plan by a vote of 79.33 per cent. It is evidence of the facts that in a general way were before those bondholders at the time each of the various proposals were put forward, and what the general situation was at the time they voted on the plan.

Mr. Gibson: In translating that to the terms of Mr. Keegan, I understand that these statements are introduced for the purpose of supporting a claim for an increased allocation of new securities to the General Mort-

gage bondholders, and not in support of a payment of cash for the general bonds. Is that correct?

Mr. Watts: No, it is not quite correct. They are not introduced for the purpose of supporting any increased securities or payment of cash, but merely on the question of the reasonableness of the vote.

The Court: Is the reasonableness of the vote on any class of securities an issue in the case?

Mr. Watts: A very important issue.

The Court: Is that in question, the reasonableness——

Mr. Watts: Yes sir. We didn't intend to come to [fol. 324] that until later.

The Court: You are referring to Exhibit——

Mr. Watts: It says in Section 77 (e) if the plan has not been accepted by the creditors and stockholders, that is, if it has not received a two-thirds vote by each of the classes entitled to vote, and that is the case here, the judge may nevertheless confirm the plan if he is satisfied and finds after hearing that it makes adequate provision for fair and equitable treatment for the interests and claims of those rejecting it. And here is the point: "that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts." And then it continues by requiring the Court to find again that it "conforms to the requirements of classes (1) to (3) of the first paragraph of this subsection." We think it is of great importance that the Court must find after hearing that the objection was not reasonably justified, and we believe these exhibits throw a great deal of light on that question of whether the objection was reasonably justified.

Mr. Gibson: I understand that these exhibits are not introduced for any additional payment on the General Mortgage bonds.

Mr. Watts: This is right.

Mr. Gibson: Mr. Keegan, I notice in column III the interest on senior indebtedness is computed according to the expressed interest rate of collateral notes, without recognizing the interest on the collateral. Is that right?

Mr. Keegan: Yes, it is my understanding that on page 32 of the last annual report that that Reconstruction Finance Corporation interest is the interest on that collateral.

[fol. 325] Mr. Gibson: And simultaneously for the Chase National?

Mr. Keegan: Yes. We simply add those columns together and subtract the interest on the General Mortgage.

Mr. Gibson: Am I correct, then, in understanding from your Exhibit 10 that interest requirements on the senior debt, even when computed in the method you followed, were not covered? There was a failure to cover them by over $16,000,000.00 from the inception of the reorganization proceedings down to the year of 1942, and it was only by including the surplus of the four years that the correct amount was computed; is that a correct statement?

Mr. Keegan: I think that would be a substantially correct statement.

Mr. Watts: That is not surplus cash. It is a statement of the earnings available.

Mr. Gibson: Thank you for giving me a better impression.

The Court: May I ask you a question, Mr. Keegan?

Mr. Keegan: Yes sir.

The Court: In the third supplemental report, which is the plan for the consolidation of the Salt Lake, the Rio Grande Junction bonds are allowed $2,121,000.00 first mortgage bonds and $634,000.00 of income bonds. Do you want those particular securities reallocated to the General Mortgage bonds? What securities do you want? Do you want a block of common stock?

Mr. Keegan: We intended to cover that in detail in our argument. The way that will work out is this. In our [fol. 326] argument we want to review some late decisions of some other railroad reorganizations where surplus cash was used to reduce senior claims and the courts have required that proper adjustments be made as we have asked here. When the Commission promulgated the plan two and three-quarter million dollars of Junction bonds were outstanding to the public, and they naturally figured they would have to use the new bonds in place of them. Now that the trustees have purchased them and the bonds have been taken out of circulation our position is that by reason of their having purchased those bonds, it is no longer necessary to issue new bonds in exchange for them. Consequently that releases two and three-quarter millions of securities in the new company for redistribution generally. The way that works out is a matter of railroad accounting. The Commission has already fixed the relative position of the parties. The way these cases I intend to review in my

argument have handled that, they just made a general distribution of those on the same basis as the original distribution, and the way it works is that we get better treatment; everybody gets better treatment. For instance, in this appendix here the First Trust 4s are originally getting seventy-three per cent in new first mortgage bonds and twenty-eight per cent in new income bonds. They will get a little higher ratio in the distribution of the new first mortgage bonds and less of the new income bonds, and on down the line everybody's treatment will be sweetened a little, and when the ones next ahead of us are sweetened they are getting less common stock and better securities, so it releases $2,758,333.00 of par value common stock at the end which becomes available for the General Mortgage bondholders.

[fol. 327] The Court: Aren't you violating the priority rule as set out in the Milwaukee case? That is a question of argument, though.

Mr. Keegan: If you want me to go into those cases to show how those courts have been doing that— They had their hearings since last fall. There have been several cases come down where they have done this very thing, and I would like to discuss that in detail and show how that works out.

The Court: Well, we will not do that now. Put your evidence in.

Mr. Keegan: I offer these two exhibits.

The Court: They have been admitted.

Mr. Keegan: That is all the evidence we have at this time, although, as I understand it, what we are doing now is trying to segregate this Junction issue. After lunch it will take about twenty minutes to argue that. We do have some broader objections, and Mr. Watts would like to have the right to interpose some evidence later on our broader objections.

The Court: Do you want to introduce that before the argument?

Mr. Keegan: Whatever you prefer.

The Court: Let's have all the evidence first.

Mr. Watts: Your Honor please, I should like to call Mr. Miles C. Kennedy.

MILES C. KENNEDY, a witness called and sworn on behalf of the City Bank Farmers Trust Company, testified as follows:

[fol. 328] Direct examination.

By Mr. Watts:

Q. Mr. Kennedy, will you give your name and address?

A. My name is Miles C. Kennedy. I live at 45 Fifth Avenue, New York.

Q. What is your profession, Mr. Kennedy?

A. I am a consulting engineer. I am a member of the firm of Coverdale & Colpitts', consulting engineers, office at 120 Wall Street, New York City.

Q. Will you please give a brief statement of your professional experience?

The Court: Is there any question as to his qualifications by anyone?

Mr. Homire: We will waive any question as to that.

Mr. Gibson: We will do likewise.

The Court: All right.

Mr. Watts: Your Honor, may I inquire whether that goes to the extent of—I hope to bring out in these qualification questions the fact that the witness and his firm have in a very large number of railroad reorganizations served as special advisers and consultants to the bondholders, bondholder committees, creditor groups and the like.

The Court: That fact is well known to the Court and I presume it is to all the parties here.

Mr. Gibson: We so admit.

Q. Mr. Kennedy, I am about to lay the groundwork for rather an important question for the General Mortgage Trustee. I will ask you whether you have examined at our request the two exhibits which have just been introduced, being City Bank Farmers Trust Company Exhibit 10 and [fol. 329] Exhibit 11, the first of which is entitled "Table Showing Debtor's Income Available For Interest And Interest Requirements For All Securities Senior To General Mortgage Bonds For Each Year During Reorganization Proceedings," and the second of which is entitled "Table Showing (a) Current Debtor's Income Available For Interest And (b) Surplus (Or Deficit) Of Total Debtor's Income Available For Interest To Last Previous December

31 Over Interest Requirements To The Same Date Of All Securities Senior To General Mortgage Bonds (Including Interest On Unfunded Debt), All As Of The Respective Dates On Which The Several Plans Were Proposed—As Well As The Treatment Proposed For General Mortgage Bonds In The Several Plans"?

A. I have.

Q. To the best of your knowledge, Mr. Kennedy, has the substance of the information which is outlined in both of these tables, and particularly the table included in Exhibit No. 11, been available to the public and to the holders of the General Mortgage bonds?

A. Yes, it has. Perhaps not in exactly this form, but it could have been arrived at by very simple computations. The income accounts are, of course, published in the daily press, and all the information in regard to the plan has been in financial papers, dailies, weekly, statistical services and the manuals which are readily available.

Q. Mr. Kennedy, in your opinion is this the kind of information which would and which should be carefully considered by the General Mortgage bondholders in determining how they should vote on the acceptance or rejection of the plan of reorganization?

A. Yes, I think it is very important information. All the relevant facts are important, of course, and these do not purport to be all the relevant facts.

Q. Mr. Kennedy, will you explain in a little more detail what you conceive to be the particular significance of Ex- [fol. 330] hibit No. 11 or the figures which are set forth in the table on Exhibit No. 11?

A. Well, I think one of the highly significant facts set forth in Exhibit No. 11 is the sum total of the accumulated surplus table arrived at in column V in line No. 12 which shows that as of December 31, 1943, the last previous year end to the submission of the plan, all the interest on obligations senior to the General Mortgage bonds had been earned with a margin of $3,859,306.00 to spare. In other words, if the amounts earned available for interest on the senior obligations had been paid to the holders of those obligations, the position of the General Mortgage would have been no worse than it was at the beginning of the receivership. Now, as compared to that, the other significant fact is shown in the percentages on column III of this exhibit, which shows that in the first plan filed, which was the debt-

or's plan, the General Mortgage was accorded 100 per cent treatment in new preferred stock, that is, preferred stock in the proposed new company. That is, they would have gotten dollar for dollar in par amount in satisfaction of their claim as of that date, of their principal amount as of that date. The next plan was the Insurance Group plan of 1937 which gave the General Mortgage 100 per cent in new common stock. After hearings before an examiner of the Interstate Commerce Commission the examiner recommended fifty per cent in new common stock. The Interstate Commerce Commission in two subsequent plans awarded thirty-three and one-third per cent. One of these was in 1939, and one was in 1940. A certain discussion plan more or less agreed upon—I don't know exactly—in 1941 again gave the General Mortgage bonds fifty per cent. The Court's [fol. 331] plan of 1941 brought the amount to 32.99 per cent, to practically thirty-three per cent, and in 1941, skipping down to line 9, the Insurance Group plan accorded the General Mortgage 47.42 per cent. Then we get along to 1942 and the Interstate Commerce Commission cut the percentage down to five per cent, and in 1943 they doubled that treatment by giving them ten per cent. Now, coupled with that fact is that the earnings of the property had been improving steadily since about 1937, when, according to Exhibit 10, there was a deficit of $249,880.00 in income available for interest. Those earnings increased very substantially, due in part I should say to the generally increasing prosperity, due in rather large part I should say to the improvements which were being made in the debtor's program, under which very large amounts were spent for improvements which it is reasonable to assume produced very substantial savings or increases in revenues.

Q. It is true, is it not, that the figure $3,859,306.00, which you referred to as the figure in column V, line 12, that is, $3,859,306.00, represented the accumulated surplus up to December 31, 1943, of the income available for interest over the interest requirements of the so-called senior obligations? It is true that the period during which that figure was built up included some abnormally good years; is that not so?

By the Court:

Q. It included war years?

A. Yes, up through 1943. Obviously those were abnormally good years, but it may also be said that some of these

years were abnormally bad years, and, furthermore, in some of these years in the period, perhaps all of them, the earnings were reduced because of the expenses incident to the very large improvement program which I just men-
[fol. 332] tioned.

By Mr. Watts:

Q. Mr. Kennedy, in referring to what might be called the deterioration in the treatment for the General Mortgage bondholders as outlined in column III of Exhibit 11, you are, of course, familiar with the fact that the total capitalization provided for in the several plans was not uniform; there were some changes?

A. Yes, I am aware of that.

Q. And although the figures do not appear in this exhibit, if I advised you that, for example, in the first Insurance Group plan, which is the one referred to in line 2 of that exhibit, the common stock which the General Mortgage bondholders were to receive constituted 100 per cent of the common stock provided for in that plan, and that in each of the subsequent plans through the Insurance Group plan No. 2 which is referred to in the ninth line of that exhibit, all of the allotments of the common stock in the various plans to the General Mortgage bondholders constituted a minimum of approximately thirty-three per cent of the total amount of common stock in the reorganized company to be issued under the plan; would that factor be of any significance to you in your answer to that question?

A. Will you let me see those figures?

Q. Yes, they are set forth in the last column on page 6 of the brief which we filed with the court last September, a year ago.

A. Well, these figures show that not only did the General Mortgage bonds get less per dollar in new stock, but that they got increasingly smaller portions of the common stock to be issued.

Q. So in a general way that fact merely increases the
[fol. 333] change or tendency shown by the other features of the plan?

A. Yes, it does.

Q. Now, Mr. Kennedy, you know, I believe, that in view of the fact that the interest on the obligations prior to the General Mortgage bonds was, taking this period up to December 31, 1943, as a whole—in spite of the fact that that

interest was earned, no interest was paid until sometime after December 31, 1943?

A. Yes, that is my understanding.

Q. Do you know what was done with the money which was earned but which was not paid out to the security holders?

A. Yes, I do in a general way. Up to the end of 1943 the trustees under the direction of the Court had expended, I think, about $37,000,000.00 in improvements, additions and betterments to the property. All of that money did not come from the accumulated earnings set forth here. Part of it came from equipment trust issues I think in the amount of some five to six million dollars. Part of it was, of course, accrued in depreciation accounting, but it is quite clear that the earnings of the property throughout this period in general have been used to improve and strengthen the property in the discretion and wisdom of the trustees and the Court.

Q. And in addition, of course, you are familiar with the fact that over the period as a whole there has been an increase in the cash and current assets over current liabilities?

A. There have been very substantial increases.

By the Court:

Q. Take that column III, Exhibit 11, which shows the amount of common stock, are those percentages, fifty per cent, 100 per cent, of the same amount of common stock?

A. No, sir, they are not percentages of an amount of com- [fol. 334] mon stock at all. They are percentages of the dollar amount of the new stock at par which is given to each $1,000.00 bond.

Q. The minimum is thirty-three per cent, and then again we have next thirty-three per cent. Thirty-three per cent of the larger amount of common stock?

A. No, I don't believe it is a larger amount, but I believe it is of a smaller amount. The figures on the exhibit, line No. 2, for instance, the Insurance Group plan of 1937 where it says 100 per cent in column III that means for every $1,000.00 of General Mortgage claims there would be distributed $1,000.00 of new common stock, that is, dollar for dollar. In line 3 where it says fifty per cent, it means that each $1,000.00 of claim would get $500.00 in par amount of new common stock.

Q. It has no relation to the total amount of the issue of common stock, has it?

A. No, but I can give you that figure if you care to have it.

Q. I just wanted to know if those figures were fifty per cent of the amount of common stock.

A. The result of these various treatments was that the proportion of the total issue of new common stock to be received by the General Mortgage became increasingly less as time went on.

Q. Take the last two there, 5% and 10%, it might be 5% of a lesser amount of total common stock, and it might be 10% of a larger amount?

A. Well, I can tell you exactly what that is. Five per cent would also have been five per cent of the new common stock. Ten per cent treatment would have amounted to twelve per cent of the new common stock.

By Mr. Watts:

Q. In other words, when the 1943 plan came out there was a slightly smaller amount of common stock authorized? [fol. 335] A. That is correct, and therefore ten per cent made a larger amount of the total.

Thereupon a recess was taken until two o'clock p. m.

Pursuant to recess the following proceedings were had at two o'clock p. m.:

MILES C. KENNEDY resumed the stand for further

Direct examination.

By Mr. Watts:

Q. Mr. Kennedy, in answer to one of my recent questions you were explaining some of the significant features of Exhibit No. 11. Now, Mr. Kennedy, assuming the correctness of your conclusion that funds were diverted from the payment of interest on secured obligations for the purpose of making large improvements in the property intrusted to the debtor's trustees, what conclusion would you or a General Mortgage bondholder be warranted in drawing from that fact?

The Court: You want him to put himself in the position of a bondholder?

Mr. Watts: Yes, your Honor.

The Court: Well, has he the right to do that? He may state what facts were before a bondholder, but what conclusion the bondholder would draw from them he can't state, can he?

Mr. Watts: Well, sir, the way I feel about it is this: that we are speaking about what would be reasonable conduct for a holder of General Mortgage bonds, and we believe that the views that Mr. Kennedy would have in the light of [fol. 336] his experience, and with his access to what is a matter of public information on this issue would be very similar to the—the conclusions he would draw would be very similar to the conclusions any normal similar person would draw. May I change it and ask Mr. Kennedy what conclusions he would draw from that fact?

Mr. Homire: If he were a bondholder?

Mr. Watts: No, just from those facts what conclusion does he draw?

A. Well, I would start out with the assumption, I believe, that the trustees of this property were acting with all wisdom and discretion not only because they were appointed by this Court and confirmed by the Interstate Commerce Commission, but because I know and I believe it is a matter of general information that the trustees have done an outstanding piece of work for this property. I would therefore believe that in diverting funds from the payment of interest to investments in the property the trustees were doing what they believed and what was for the benefit of the debtor's estate and for the security holders for whom they were trustees. From that I draw the conclusion that they considered the investment of this money in additions and improvements much more beneficial to the security holders of the company than the payment to them of current interest, because I do not believe that they would do anything to worsen the position of their security holders or any class of them; certainly not willingly. Now, of course, it is reasonable to believe that the expenditures that these trustees made have been productive and will be productive of very substantial earnings. I spent several years with the Pennsylvania Railroad making economic studies of the [fol. 337] savings it had out of new work, the added traffic

to be obtained by new lines and extension of lines, and I know very well an improvement that didn't earn fifteen per cent on its cost or was not estimated to earn fifteen per cent on its cost would receive no consideration whatever from the management, and I therefore assume that these improvements or most of them could be expected to earn ten per cent to fifteen per cent or even more in some cases. Now, if that is the case the position of the bondholders is improved, and even though money has in effect been borrowed from the bondholders through the non-payment of interest, which has been used for making improvements, there is bound to be considerable income in excess of the interest that will be paid on that money when interest is again resumed, and that benefit would flow down to the junior issues in the reorganization. I should therefore conclude that the position of the General Mortgage—what I have already said is true—the position of the General Mortgage should be better rather than worse through the expenditure of this money by the trustees even though it has meant the piling of additional debt ahead of the mortgage.

By the Court:

Q. Assuming that this expenditure is proper, would it not be better today not to pay the interest and make the improvements than to go out and borrow money to make the improvements?

A. Of course, I take the position you are borrowing the money anyway which has been earned by your bonds, and you are retaining it and not paying it out to them——

Q. Are they entitled to the earnings of the road until the road is properly maintained; all of the earnings except [fol. 338] those necessary for the maintenance of the property?

A. I am not talking about maintenance. I am talking about improvements over and above the maintenance.

Q. What improvements were not necessary in order for the company to earn income?

A. You could have replaced various parts of the property in kind. Instead of that you went out and built better bridges than you had before. You bought better equipment than you had before. Understand I am not criticising in any way any part of this program. Relying upon the trustees, as I said, I have no inclination to criticise anything that was done. I am saying, however, that the

money that was used to make a substantial part of these improvements was in effect borrowed from the bondholders and claims piling upon the reorganization on which interest will be paid.

Q. How were they denied this money if there wasn't money enough to make improvements and also pay interest? Are the bondholders entitled to these earnings at the expense of the maintenance of the property?

A. I wouldn't give them credit for one cent over the earnings of the property, but I draw a sharp distinction between the earnings of the property and the maintenance because the ICC makes a distinction in them.

Q. What on this property are the improvements? Don't you think it is better to put in the heavier rail in order to carry on its work and do a good job?

A. Yes sir, I do.

Q. And if it hadn't done a good job they would not have been earning anything at all? They would have been sunk as they were before the reorganization.

[fol. 339] A. That is quite possible. I think the earnings of the property have undoubtedly improved because of this program, but nevertheless the records show that very substantial amounts were spent for additions and betterments which were over ordinary maintenance, and it is my view, whether I am correct or not, that the bondholders, unless they acquiesced in that move, would have had the right to come in and protest against the expenditure of this money for improvements as against paying interest on their bonds.

Q. Is there any law supporting that position, do you know?

A. I don't know, sir.

Mr. Hodges: I can cite you a case in the Third Circuit Court of Appeals. I will give it to you.

The Court: Very well.

By Mr. Watts:

Q. Mr. Kennedy, you spoke before of a substantial improvement in the debtor's cash position as of December 31, 1943. Can you tell me what the cash position was on that date? I believe that is in the report of the trustees.

A. I have it here somewhere. If you will give me that 1943 report that Mr. Thompson introduced——

Q. Yes (handing document to witness).

A. From page 12 of this Exhibit No. 8 which Mr. Thompson introduced this morning, the cash as of December 31, 1943, was $12,716,924.00. Temporary cash investments were $8,005,000.00. Total current assets were $33,915.00, roughly, and current liabilities were $23,517,000.00, also roughly, which gives net working capital of approximately $10,400,000.00.

Q. Were there also shown special deposits aggregating a [fol. 340] little over $609,000.00?

A. That is true, but I haven't mentioned them because Mr. Thompson brought out this morning they were definitely earmarked for special purposes.

Q. Mr. Kennedy, in view of the cash distributions which have been and were being provided for security holders in numerous other reorganization proceedings before the Interstate Commerce Commission and before the courts, was it in your opinion reasonable for the General Mortgage bondholders to assume that some of this cash to which we have just been referring might be used to reduce accrued interest on obligations prior to the General Mortgage bonds, and thus improve the position which the General Mortgage bondholders might expect in the plan of reorganization?

A. Yes, I think so. I can think of several cases where cash distributions were made to reduce claims, and those cases, generally speaking, received rather wide publicity, and it would be quite natural for bondholders not only in this company but in other companies to expect or have strong hopes that similar distributions would be made in these cases.

Q. I come now, Mr. Kennedy, to the question for which I have been laying the groundwork by these previous questions, and first I want to read again certain language of subsection (e) of Section 77 of the Bankruptcy Act, which says that; "if the plan has not been so accepted by the creditors and stockholders"—that means by the vote of two-thirds of each class of securities entitled to vote—"the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing,"—then I will skip a little—"that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the [fol. 341] relevant facts." Without reading the balance of these requirements, in your opinion, based upon your general experience in such matters and upon the testimony which you have just given, was the rejection of this plan by

the General Mortgage bondholders reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts?

Mr. Gibson: Your Honor please, that forces an ultimate question of law. The statute implies whether your Honor is satisfied, not whether Mr. Kennedy is satisfied. We doubt if the witness is competent to express an opinion on that ultimately.

The Court: I think the objection is good, but I will let him answer if you want it in the record.

Mr. Watts: We are just asking his opinion.

The Court: You are asking his opinion how someone else should make up their minds. He can answer, but I don't know what value it will have.

A. In my opinion it was.

Q. Mr. Kennedy, I have here a five page pamphlet which is entitled in black letters "H. R. 2857," and in smaller type "78th Congress 1st Session." It appears to be a copy of a bill which was introduced in the House of Representatives on June 3, 1943, by Mr. Hobbs, and to have as its purpose the amendment of Section 77 of the Bankruptcy Act. According to the heading it was referred to the Committee on the Judiciary. Will you examine that (handing document to witness).

A. Do you want to ask me a question about it?

Q. Are you familiar in a general way with the text of that [fol. 342] bill?

A. Yes.

(Thereupon a document was marked for identification City Bank Farmers Trust Company Exhibit 12.)

Q. Mr. Kennedy, on the first page of that bill, beginning on line 8, will you read beginning line 8 of page 1 through the tenth line of page 2?

Mr. Homire: Your Honor, we object to any reference to this bill in the record. This is a bill which has been postponed and has not even been passed by either house of Congress, has no relevancy whatever to this case, and we object in the proceedings here.

Mr. Gibson: I think it is hard enough to operate under Section 77, much less something that has not been passed.

Mr. Watts: We are attempting to show here whether the action of the General Mortgage bondholders by voting by a vote of about four to one of those voting to reject the plan was something reasonable, whether it was reasonably justified in the light of all the relevant facts. This bill and the subsequent versions of it and the report of the Committee on the Judiciary, which was a unanimous report and which I want to offer later, was a matter which was widely publicized in the daily press. They are matters of which the bondholders may be expected to have had general knowledge. It would have had a great deal of effect on what their rights would be under a plan of reorganization, and I believe it has a very great bearing on the question of the reasonableness of their vote.

[fol. 343] Mr. Gibson: It may be natural and human to hope that something will turn up, but it can hardly be reasonable to rely on a bill which is so obviously doomed to rejection as this bill is.

The Court: The Court will take judicial notice that this bill has not been passed, and when offered there was a strong reaction against it. I would also want to get the advice there of the bondholders or the trustees or anyone else who was interested in it.

Mr. Watts: We propose to ask that ourselves.

The Court: I think I will sustain the objection. You may use it in your argument if you wish.

Mr. Hodges: May I suggest to your Honor that it is something of which your Honor can take judicial notice. There is a unanimous report of the House Judiciary Committee, giving its views on the meaning of Section 77 as it was originally passed.

Q. Mr. Kennedy, you are also familiar with subsequent versions of this bill which were variously referred to, H. R. 4873 of the 2nd Session of the 78th Congress, H. R. 4904 of the 2nd Session and H. R. 4960 of the 2nd Session?

A. That is correct.

Q. And from your general familiarity with the texts of these four bills do you know whether they related to substantially the same subject matter?

A. Yes, the substance is about the same.

Q. Are you also familiar with a twelve page pamphlet which I am now handing you, which is entitled "House of Representatives Report No. 1615, 78th Congress, 2d Ses-

sion,'' and which appears to be a report from the Com-
[fol. 344] mittee on the Judiciary, stating that H. R. 4960 as amended, having been considered, is reported favorably to the House with the recommendation that it do pass? Are you familiar with this report?

A. Yes, I am.

Q. And with the fact that it is stated in the report that it is unanimous?

A. Yes.

Mr. Watts: Your Honor, I suppose that this report would be subject to the same objection.

Mr. Gibson: We make the same objection.

Mr. Watts: I would like, however, for the purpose of the record to offer it and have it marked as City Bank Farmers Trust Company Exhibit 13 for identification.

The Court: Well, I have just found an extract here from a Los Angeles case where the Supreme Court said "The question of whether a plan of reorganization is fair and equitable is one of law, and the fact that the great amount of security holders vote against it is not the test. A plan can be approved by the Court that is fair and equitable even though the record number of security holders object." I suppose the opposite of that is true. You are arguing here that your client did not approve of this plan; that it disapproved of it.

Mr. Watts: Now we come to the question of whether the Court should confirm the plan over their objections, and that is quite a different question than whether the plan is fair and equitable. I am not offering this testimony on the question of whether the plan is fair and equitable. We [fol. 345] are offering this testimony on the question of whether the action of the General Mortgage bondholders in voting against the plan was reasonable in the light of the situation as it existed on that day; that is, in the light of all the information they had, whether on the basis of that they were reasonably justified in so voting.

The Court: You haven't offered any testimony that the security holders you mention knew of the Hobbs bill or it was called to their attention, or that they were influenced by it.

Mr. Watts: Well, sir, I propose to come to that. I am going to cover that in my questions to a later witness. I have here a man who has been consulted by a great many

of them, who has had to meet their inquiries and their complaints, and who knows from the telephone calls, from the letters he has received, that, generally speaking, holders of General Mortgage bonds of this road did know it.

The Court: The Court will take judicial notice of the fact that every stockholder who thinks he has been gyped thinks the Court has taken some action.

Mr. Watts: I think we are narrowed down to the question of whether our bondholders were reasonably justified in their vote, which is quite a bit different from whether this bill will become law or whether it should become law, or whether, it pending, it was reasonable for the bondholders to vote against it.

The Court: According to this Los Angeles case the Court shouldn't be influenced by it.

[fol. 346] Mr. Watts: That is on the reasonableness of the plan.

The Court: It is a distinction without a difference.

Mr. Watts: If there were no distinction it would not be necessary to provide for this second hearing on the vote. As we see it, first this matter came up on the question of reasonableness of the plan. Now, the Court has the right to decide on the reasonableness of the rejection. In the previous hearing we said the General Mortgage bondholders did not believe the plan was fair and reasonable. We argued this orally and we argued this in our brief. This Court decided differently. We believe it was proper for this Court to decide either way. It was a question on which reasonable men might differ, but when you get to this next question of whether this Court may confirm the plan over the objection of a great majority of one class of bondholders, we have something that is entirely different. Now, this Court under the statute must review the action it took last year, and, after hearing, it must again find that the plan was fair and reasonable. That is the first part of this provision. After it has done that, the Court must say "Well, then, I not only find that the plan is fair and reasonable but that you are not reasonably justified in thus rejecting it." That question was not under consideration before. Then the Court must find that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts. If your Honor please, the General Mortgage Trustee found no case, [fol. 347] either under Section 77 (e) or any other statute,

where a holder of a secured claim has been required to surrender his claim and the security for the claim, and to accept something else in exchange for his claim over his objection without at least a majority vote of approval from other secured creditors of the same class. We believe that it is not proper for a court under any statute to confirm a plan over such objections without at least a majority vote of approval. That would relate to a reorganization under Section 77 of a bankruptcy composition. It is fundamental that you cannot take security from a man or make a secured creditor release his claim unless a majority think it is fair under the circumstances and vote for it. Here we haven't got that. We have approximately eighty per cent of the bondholders voting against this. That in itself is evidence of the reasonableness of their rejection. If it were by a smaller vote it would not be nearly as persuasive. This Court must find that they had no reasonable basis, no sound basis, for voting against it, before it can confirm the plan over their rejection even though it was proper before to find the plan fair and reasonable. This is a very serious thing.

Mr. McAllister: Mr. Watts, may I ask you a question? You have said eighty per cent of the General Mortgage bondholders voted against it. That was only about seventeen per cent of the votes.

Mr. Watts: Only about four per cent voted in favor, so it was about four to one voted against the plan.

The Court: What percentage of all the bondholders were represented?

Mr. Watts: That is, those that voted for and against [fol. 348] the plan?

Mr. McAllister: I think, your Honor, it is about twenty-one per cent of all of the bondholders voted either for or against the plan.

Mr. Gibson: May I supplement that, your Honor? The exact figures are that of the outstanding General Mortgage bonds less than twenty per cent, approximately seventeen per cent, voted against the plan, and of all publicity held bonds, which was your Honor's exact question, 4.64 per cent voted for the plan, only 4.64 per cent, and could I say that by not answering Mr. Watts at this moment we do not want to be in the position of seeming to agree to any of the argument he has made?

The Court: I understand. We will take the testimony and discuss this later. Finished with your witness?

Mr. Watts: Your Honor, may I ask the witness to read these provisions before you make your ruling, so we will have them in the record?

The Court: What provisions?

Mr. Watts: The provisions of the proposed statute and the sections of the Executive Committee report.

The Court: I don't think I am interested in that. I don't think proposed legislation is any evidence at all or should have any influence on the Court in the decision of the case, unless you bring it home to each individual bondholder and have him here and have him testify he was influenced by the argument in support of the bill or the provisions of it.

Mr. Homire: Your Honor, right at that point I think it would be desirable to point out that the statute provides that the Court fail to confirm the plan if the rejection was reasonable in the light of the rights and interests of the [fol. 349] bondholders so voting to reject, not in the light of their rights at some future time or following the passage of some future legislation. Even if they knew all about this legislation it would not be ground for your Honor sustaining their vote of rejection.

Mr. Watts: Your Honor, that goes just part way through that section. It is "in the light of the respective rights and interests of those rejecting and all the relevant facts," and we believe that the fact that there was such legislation pending was a relevant fact. It might influence them. They were considering all reasonable evidence.

The Court: I suppose you could go through the bills of Congress and find bills about everything. I don't think this has any bearing at all.

Mr. Watts: All we are urging is that the bondholders when they voted knew that such a bill was pending, that it had been unanimously approved by the Committee on the Judiciary, and we believe that has a bearing on whether or not the rejection was reasonable.

The Court: What evidence have you that it was approved by the Judiciary Committee? You haven't any members of the Judiciary Committee here, have you?

Mr. Watts: I have an official publication here.

The Court: I don't think I am interested in that, going into all the matters proposed before the Congress and some

committee. If you want to submit it in a brief I shall be glad to consider it.

Mr. Watts: And to obtain your ruling I would like to offer the exhibit which has been marked City Bank Farmers Trust Company Exhibit 12 for identification—Exhibit 13 for [fol. 350] identification.

The Court: I will sustain the objection.

Q. Mr. Kennedy, do you know when the present plan was submitted to the holders of the General Mortgage bonds for acceptance or rejection?

A. April of this year I understand.

Q. If I tell you the official——

A. It was April 26, 1944.

Q. Does that refresh your recollection?

A. Yes sir.

Q. If I tell you that in the paper submitting the plan it was stated that the votes must be in by June 10, 1944, would that refresh your recollection on that?

A. Yes sir.

Q. Do you know if any notice regarding the introduction of the Hobbs bill appeared in the daily press?

A. It was covered pretty well in the financial page of the papers that I read. That is as far as my knowledge goes.

Q. Do you know whether the bill was the subject of discussion among persons interested in railroad reorganizations generally?

A. Yes, it was.

Q. In view of the pendency of the bill, the nature of its provisions, in your opinion was the vote of the General Mortgage bondholders in rejecting the plan reasonably justified?

A. I would say it was reasonably justified——

Mr. Gibson: That is the same question.

The Court: What was the question?

(Question read.)

The Court: Objection sustained.

Mr. Watts: If your Honor please, that is all the questions I have of this witness.

The Court: Cross-examination, gentlemen?

[fol. 351] Cross-examination.

By Mr. Gibson:

Q. Mr. Kennedy, your Exhibit 10 or City Bank Farmers Trust Company's Exhibit 10 refers to the insurance Group plan as originally proposed. Will you tell me whether or not it is a fact that in that plan the Refunding and General Mortgage bondholders and the holders of all bonds senior in position to them, or equal in position to them, if there are any, were recognized to the full amount of their total claim in preferences, or whether——

Mr. Watts: I think you made a mistake in that, Mr. Gibson.

Mr. Homire: Are you referring to the General Mortgage?

Q. I again state to you as a matter of fact, Mr. Kennedy, that aside from the General Mortgage bonds every bondholder received in the Insurance Group plan the total amount of his claim, the total amount of his claim or better?

A. I think that is true.

Q. Is it not also true in the second Insurance Group plan the senior bondholders received more advantageous treatment than they finally did in the plan now before the Court?

A. I can't answer that, Mr. Gibson. I haven't given any particular consideration to the treatment accorded to other bondholders as among themselves or in total.

Q. If I would state to you as a matter of fact that a larger allocation of new First Mortgage bonds was made in that plan to existing senior creditors, would you be able to deny that?

A. No, I would not. I would not be able to express any [fol. 352] opinion on it at all.

Q. So it follows that the General Mortgage bondholders are not the only ones who didn't get bonds much as they hoped they might; isn't that true?

A. I don't know, Mr. Gibson. Are you asking me to state what may——

Q. If those premises are right, the conclusion is right; isn't that so?

A. That is true.

Q. In your City Bank Exhibit 10, I believe it is, the percentages are shown on the total claim of General Mortgage

bonds recognized in the new common stock allocation. Is it not true that that percentage is computed on the basis of total claim, and not on the basis of principal amount?

A. Yes.

Q. Is it not true that from that it would necessarily follow that the mere lapse of time would itself reduce all percentages even if no change were made in the allocation?

A. Yes.

Q. Is it not true that the General Mortgage bonds are the most junior security that is recognized in the plan?

A. Yes sir.

Q. Is it not also true that the most junior claim is not always allowed interest?

A. Yes, the junior recognized security in general takes what is left.

Q. Is it not also true that if that percentage were computed on the basis of principal amount in general it would be 14.61 instead of 10?

A. I think that is true.

By Mr. Hodges:

Q. Is it not also true, Mr. Kennedy, that taking your Exhibit 11, column III, and the percentages beginning at the bottom of that column with the ten per cent and going upwards, that your percentages would be altered if they [fol. 353] had reference to the original claim of the General Mortgage, unaffected by the accumulation of interest?

A. Yes.

Q. And you haven't figured it on that basis of the principal of the General Mortgage claim as it existed on November 1, 1935?

A. I haven't, Mr. Hodges. I don't know if anyone else has or not.

Q. Are you acquainted with the amount in principal, the principal amount of the senior claims against this debtor as of November 1, 1935, senior to your General Mortgage?

A. Well, I have seen the figures, Mr. Hodges, but I haven't got it in mind.

Q. Accuracy is not necessary to this inquiry.

A. Well, my memory is notoriously poor, Mr. Hodges, and I wouldn't want to hazard a guess. (Referring to document) Well, something in excess of $100,000,000.00 I would say from this computation, that is, principal amount.

Q. That is the principal amount of what might be called senior claims in the aggregate of $101,970,000.00?

A. Yes sir.

Q. And that figure represents the principal amount of all of the bond issues in the hands of the public and all of the bonds pledged and the obligations for which they were pledged?

A. That is my understanding.

Q. And that the total will amount to $101,000,000.00 or approximately $102,000,000.00? That is close enough for our purposes.

A. Yes sir.

Q. And on that day, November 1, 1935, there were $102,000,000.00 of obligations ahead of you. I am speaking of you now as a representative of the General Mortgage bond-[fol. 354] holders. Have you looked at this record in these proceedings to see what valuations have been used by the Commission?

A. Yes, I have.

Q. They have expressed something in terms of capitalization, and do you take it that that is the way they have of expressing some idea of value?

A. You mean the total capitalization?

Q. Yes.

The Witness: May I have that question, please?

(Question read to the witness.)

A. Yes.

Q. So that for the purposes of this questioning I will use capitalization in the sense of value. Do you know of any capitalization that they suggested at any time in any plan that was less than $140,000,000.00?

A. You mean for this property?

Q. Yes, for this railroad.

A. No, sir, I don't.

Q. And what was the principal of your debt on November 1, 1935?

A. In the neighborhood of twenty-nine million.

Q. Twenty-nine million. So, taking your twenty-nine million to the one hundred and one million ahead of you, there was one hundred thirty million of debts to be compared with the one hundred and forty million capitalization?

A. That is correct.

Mr. Gibson: By that you mean principal amount?

Mr. Hodges: I mean principal amount of debt on November 1, 1935.

Q. So that if this plan of reorganization had been put into effect on November 1, 1935, on the basis of any valuation that has been used in this proceeding your claim would [fol. 355] have received at least 100 per cent in new securities or shares under that capitalization?

A. I should judge so, yes, sir.

Q. Now we are nine years or thereabouts later. How much indebtedness are they putting ahead of you now in this plan of reorganization which is now before the Court?

A. (Referring to documents) I should say about $140,000,000.00. That is Rio Grande securities alone, not the Denver & Salt Lake.

Q. Well, using a figure comparable with the first figure you used. I think that first figure you used——

A. One hundred and forty million.

Q. That one hundred and two million was a Rio Grande figure without the Salt Lake?

A. That is right.

Q. Now they are putting $140,000,000.00 ahead of you. So that through lapse of time they have allowed to be accumulated on creditors' claims ahead of you and other creditors some thirty odd million dollars?

A. Yes, sir.

Q. And that has reduced your distributive share in the securities of this reorganization?

A. It has unless the capitalization is increased to allow for the improvements they have made, also been made during this receivership period, which have added to the value of the property, and certainly have added very substantially to its earning power.

Q. But they have not increased the capitalization over and above the original capitalization by more than $7,000,000.00?

A. That is correct, sir.

Q. And the result is that you are shoved down below thirty million more than would have been the case on November 1, 1935?

[fol. 356] A. Yes, sir, that is correct.

Q. So that during this administration the relative rights of creditors have been shifted and adjusted by the accumulation of interest on the claims senior to yours?

A. That has been the effect.

Q. That is clearly the effect, is it not?

A. It seems so to me, Mr. Hodges. I am not answering any question that has a question of law in it.

Q. There is no question of law in it. This is just the question of mathematics and the fact I wanted you to put on the record. So that starting out on November 1, 1935, you would have securities representing $100,000,000.00 of the capitalization of this new company, and today you are offered securities of a junior type representing a little over $4,000,000.00 or approximately $5,000,000.00; is that not so?

A. Yes, sir.

Q. And that latter figure is fourteen per cent of your original claim?

A. Yes, sir.

Q. And during this time this property has been improved very substantially?

A. Yes, sir.

Q. Do you know the figures of the improvement program, what has been invested?

A. Yes, there has been approximately thirty-seven million, as I recall, invested from the date of receivership to the date of December 1, 1943.

Q. Now, I would like to get very clearly with you what you meant by your discussion with the Court as to these earnings. We have before us for every year a statement of net income which you have seen I take it?

A. Yes, sir.

Q. For every year of the operation of these trustees, [fol. 357] and before reaching that figure of net income, all maintenance expenses are deducted from income; is not that true?

A. That is correct.

Q. So we have a series of years in which we have some net income, except one year I think we have a deficit?

A. You mean no income available for taxes I presume?

Q. Available for taxes, not available for interest.

A. Yes.

Q. When you say that the earnings belong to the creditors, you were talking of that income over and above all those expenditures?

A. Including maintenance, yes, sir.

Q. Yes; including maintenance. Now, you were not talking about the question of the Court's policy in improving the property and using the income to pay for that im-

provement. You were not discussing that at all except as an element of improvement; isn't that true?

A. Yes, sir.

Q. So that if any of this income over and above that net income is subject to disposition by the Court without accounting to the creditors, you didn't intend to pass on that at all?

A. Oh, no, certainly not.

Q. Now, in this period of improvement of this property I understand your testimony to be that there has been an actual improvement in the useful value of this property. Maybe I shouldn't use the word "value." In the utility of this property.

A. Yes, sir, I think very definitely that is true. To form any other conclusion you would have to conclude that the trustees had not known their business, didn't know what they were doing.

Q. The other conclusion would be that the expenditures were unjustified?

A. Yes.

[fol. 358] Q. Now, have you given consideration to a program of abandonment of rail during that period?

A. Abandonment of line?

Q. Yes.

A. I know that lines have been abandoned. I haven't any schedule of it, no sir.

Q. Have you looked at it enough to give some opinion as to whether the abandonment of these lines has improved the general efficiency and utility of the plant?

A. I wouldn't have to look at it, Mr. Hodges. I know perfectly well that the Interstate Commerce Commission approves the abandonment of a line which means that line has been a decided drain on the system, and therefore the abandonment has meant an improvement to the property.

Q. And that has been accepted as a sound proposition, has it not?

A. Yes.

Q. And then one other item occurred to me as you were testifying. You are aware, are you not, that these expenditures for what we will call additions and betterments were made during what we call the depression period or during the period of operation by these trustees?

A. During the period of operation of these trustees, yes sir.

Q. Do the men in your profession have a common understanding as to what the depression period is or was?

A. I am afraid not, sir.

Q. You can't cut it off and say the beginning was in the year 1930 or 1931?

A. No sir, because it was different for different industries, and that would always be the case. Of course, we know when the worst of the depression was, and that was in the period of 1932 say through 1935. About the middle of 1936 conditions began to improve and continued to improve through 1937 to August or September, 1937, and [fol. 359] then began to drop off again.

Q. So that these expenditures which were made between 1935 and we will say 1941, is it fair for me to say they were made during the depression period?

A. I wouldn't include 1941. I would take it through 1939.

Q. Now, does the reflection of the expenses that were incurred in carrying out such a program—does that burden fall comparatively more heavily in years of that kind?

A. You mean larger in proportion to the gross revenues, of course.

Q. And they show more emphatically in the earnings of those years?

A. Yes, dollar for dollar, that is, they do.

Q. Now, I don't know whether you want to discuss this point or not, but I want to bring it out from examination. I asked you if you knew anything about the formula used here, and you said no, and you didn't want to study it or didn't want to know it. I think there are some simple facts that you may call to the Court's attention. You do know that a test year was used, and a formula for the distribution of earnings was arrived at?

A. Mr. Hodges, all I know, or I did know considerably more about it at the time, but the only thing that I know is what I have learned from those statements of the Interstate Commerce Commission which disclosed the formula that was used. I can't discuss anything which is not in this formula.

Q. I think there are some things which you can make quite clear to the Court. I won't ask your whether the plan is good, bad or indifferent, because you haven't undertaken to determine that, but you do know from an examination of the report that a formula was used?

[fol. 360] A. Yes. I don't know how much remained of it after all the adjustments were made, but I know there was a basic formula.

Mr. Gibson: Would it not be sufficient, your Honor, that the witness has said he doesn't know?

The Court: Doesn't know?

Mr. Gibson: Doesn't know the answer to the question that is being repeated over and over by the counsel.

The Court: I think we should know it if he doesn't know.

Mr. Hodges: I will tell you what I want to prove. Maybe they will admit it. That in this formula——

The Court: What formula; the Wyer formula?

Mr. Hodges: It was originally proposed by Mr. Wyer. It was employed and adopted by the Interstate Commerce Commission, and it didn't stand on the authority of Mr. Wyer's testimony. It stood upon its adoption by the Interstate Commerce Commission, and it was a formula which is used by the Interstate Commerce Commission for the distribution of securities under this plan.

The Court: Did the Commission say they followed that formula?

Mr. Hodges: That is what I take it they say. I will refer you to the page.

The Court: All right.

Mr. Hodges: Now, it is perfectly plain that in making up that formula there is $126,000,00 of income from the Junction bonds or from the Junction property included in [fol. 361] the formula, and that the ratios of distribution are determined after putting that $126,000.00 into that formula. Now, when you eliminate the Junction bonds you eliminate that $126,000.00 from the formula, and you make the distribution to everybody less, and it is just as plain as day and it is purely a matter of mathematics, and I can argue it from this record, but I thought I would like to have this man clarify it as he could do if I called it to his attention. That is all.

Mr. Gibson: Wouldn't his argument on the record be equivalent to having it from the witness?

The Court: Mr. Hodges has ceased his examination, so we are through with that.

Mr. Watts: Before the witness goes down from the stand, it is understood, is it not, that there is no need for noting our objections to the Court's rulings or our exceptions, so that the exception is saved?

The Court: Yes.

Mr. Watts: I would like to call Mr. Ralph E. Morton.

RALPH E. MORTON, being called and sworn as a witness on behalf of the City Bank Farmers Trust Company, testified as follows:

Direct examination.

By Mr. Watts:

Q. Mr. Morton, will you give your name and address?

A. R. E. Morton, 22 Williams Street, New York City.

Q. Mr. Morton, what is your business?

[fol. 362] A. I am one of two vice-presidents in charge of the Corporate Trust Reorganization Department of the City Bank Farmers Trust Company, having been assigned to that department in May, 1927.

Q. Do you have as part of your personal work in that department the administration of trusts created by railroad mortgages?

A. I do.

Q. Has City Bank Farmers Trust Company had many railroad mortgage trusteeships?

A. It has. At the present time I am administering approximately seventy-five railroad issues in my division of the department.

Q. Do you know if the trust company, either under its present name or its former name of The Farmers Loan & Trust Company, has taken part in many railroad reorganizations?

A. It has.

Q. In the course of the work you personally have done in connection with the reorganization of corporations which have given mortgages to the trust company, have you been consulted frequently by the holders of the securities with respect to the merits of plans of reorganization or readjustment which have been from time to time proposed for the securities?

A. I have in a great many cases.

Q. Do the holders of railroad bonds frequently give you their views with regard to the fairness of proposals for reorganization or readjustment of railroad debt?

A. They do where reorganization is involved, very often at some length.

Q. They do that by letter or telephone or by calling upon you?

A. Very often by calling either personally or through legal or financial representatives or railroad experts, and also by telephone inquiries and letters.

[fol. 363] Q. Will you describe briefly some of the railroad reorganization proceedings in which you personally have participated?

A. In the last ten years I have been working on the Chicago, Milwaukee, St. Paul & Pacific reorganization, Chicago & North Western, the Erie, New York, New Haven & Hartford, the Minneapolis & St. Louis, Savannah-Atlanta, the Missouri Pacific, and I think that covers a fair part of the list.

Q. And in all those cases have bondholders consulted with you and given you their views in regard to proposals that have been made from time to time?

A. They have without exception.

Q. Mr. Morton, are you familiar with the exhibit which was introduced this morning as City Bank Farmers Trust Company Exhibit 10 which is a table of income available for interest and interest upon certain senior securities?

A. Yes, I am.

Q. And are you also familiar with the table which was introduced as City Bank Farmers Trust Company Exhibit 11 which refers to some eleven reorganization proposals which have been made in this case as well as the provision made for the claims of the General Mortgage bonds in those proposals, and set alongside of them certain figures in regard to the current earnings of the debtor available for interest in the years in which the proposal was made, as well as the net situation up to the last previous December 31st prior to the date on which such proposal was made with respect to such earnings available for interest as contrasted with such senior interest requirements?

A. I am.

Q. And have you been from time to time, as the various figures were available, in a general way familiar with all the figures which are for convenience set forth in tabular [fol. 364] form on those exhibits?

A. I have.

Q. And have you ever considered the relationship between the several treatments proposed for the General Mort-

gage bondholders from time to time as contrasted with what appear to be the current earning situation of the debtor at the time those proposals were made?

A. Yes, I have.

Q. And likewise have you considered what the net result of operations to date was to the last previous date as to which cumulative figures were available, say the last December 31st?

A. Well, I have been following the earnings monthly, Mr. Watts.

Q. From your communications from bondholders, whether in the form of personal visitations, telephone conversations or letters, do you believe that at least some of the bondholders have considered the proposals made for the General Mortgage bonds in the light of those figures?

A. Oh, I am certain they have.

Q. In your opinion does the current earning situation of a railroad generally have any bearing upon the reasonableness of a proposal to the creditors of that railroad, particularly where it is a proposal that such creditors should accept in a plan for reorganization securities different from what they hold?

A. Well, in my opinion the earnings have some bearing.

Q. And does the result of operations to the last practicable date have a bearing upon the reasonableness of the proposal made?

A. Yes, I think so.

Q. Did you, Mr. Morton, or anyone else in the Corporate Trust Department of the City Bank Farmers Trust Company make any recommendation to any holder of General [fol. 365] Mortgage bonds as to how they should vote on this plan of reorganization?

A. The City Bank Farmers Trust Company as Trustee under this General Mortgage made no recommendation to any bondholder as to whether he should vote to affirm or reject the plan.

Q. Can you state briefly why you followed that policy?

A. Well, we had been making recommendations before the Commission and Court over a period of years on behalf of bondholders. We had been approached I suppose a half dozen times by various groups of bondholders who were giving consideration to the formation of a protective committee for the bonds. We have offered them all encouragement in each case to go ahead with the formation of the

committee. After the plan was approved by the Court we thought that it was only appropriate to let the bondholders decide on the basis of their individual circumstances as to whether or not they wished to accept or reject the plan.

Q. So the vote of 79.33 per cent of the General Mortgage bondholders who voted to reject the plan was not based in any way upon any recommendation by the Mortgage Trustee that they should vote against the plan?

A. It was not.

By the Court:

Q. What did you mean when you said by their individual situation? What did you mean by that?

A. Some of these bondholders, sir, have been holding bonds which cost them upwards of par. On the other hand, there has been a speculative interest in the bonds, and in some cases some of the bondholders had a substantial profit in the bonds even at the very low price at which they were [fol. 366] selling, and we didn't deem it appropriate in this instance to suggest to any bondholder how he should vote on the plan. There was a good deal of pressure brought to bear on us to appeal from the approval order. In fact, several substantial bondholders made demands on us to that effect. In those cases we indicated that if the bondholders cared to organize and to direct us to appeal and furnish suitable indemnifications under the general provisions of the mortgage, that we, of course, would comply with their direction, but otherwise we thought it was appropriate for the bondholders to express their opinion on the plan on the ballot.

Q. When you spoke of their individual situation that would mean each bondholder should decide from his own financial situation, and not from the good of the company or the reorganization plan?

A. Well, I think he probably would decide on the basis of what he felt was his fair and equitable interest in the situation. It is conceivable that a bondholder who bought these bonds at two, when they moved up to five might feel it was a good plan.

Q. Did they ever sell them at two?

A. I am under the impression they sold that low. At least they sold between two and three, but with these very drastic plans of the Commission which have come out

very recently, the price of the bonds dropped very radically.

Q. He would be interested then whether he had a profit, and not whether it was for the good of the property? His view would then be influenced by whether he bought it at the higher price?

A. I don't know that I should endeavor to go into his motives.

Q. That is what Mr. Watts is asking you, what interest [fol. 367] these people have in voting for the plan.

A. Well, we didn't go into that. That was my answer to his question, sir.

The Court: All right. Go ahead.

By Mr. Watts:

Q. Did the General Mortgage bondholders ever come to you to tell you their views upon the plan, and to urge you to appeal from the order approving the plan, or in any cases did they tell you their views with regard to their prospective vote on the plan?

A. Yes, but I don't believe a single bondholder advised how he was going to vote on the plan.

Q. Mr. Morton, on the basis of the facts which for convenience are arranged in tabular form on those two exhibits, and on the basis of all the information that was available to the bondholders from time to time, was it in your opinion reasonable or unreasonable for the bondholders to vote to reject the plan?

A. Yes, reasonable.

Mr. Gibson: Your Honor please, an objection to the preceding question of the preceding witness was sustained.

Mr. Watts: No, it was not sustained.

Mr. Gibson: I object on the ground that the question is calling for an opinion on an issue for the Court to decide.

The Court: Objection sustained.

Q. Mr. Morton, did you hear the testimony given by Mr. Kennedy a short time ago with regard to the Hobbs bill and the report of the Committee on the Judiciary on the Hobbs bill?

A. I did.

Q. Are you also familiar in a general way with the various texts of this bill as from time to time introduced in the [fol. 368] House of Representatives?

A. I am.

Q. And are you familiar with the report on the bill?

A. I am.

Q. From your contact with holders of General Mortgage bonds do you know whether at least some of the holders of General Mortgage bonds were prior to June 10, 1944, familiar with the provisions of the Hobbs bill?

A. They were.

Q. And with the reports on the contents of the report of the Committee on the Judiciary?

A. They were.

Mr. Watts: Your Honor please, with this additional testimony as to the Hobbs bill and the report of the committee having been familiar to at least some holders of General Mortgage bonds, I should like to now reoffer the documents which have been marked Exhibit 12 and Exhibit 13 for identification.

The Court: Well, the evidence is that they were familiar with it, but there is no evidence whether they approved of it or believed in it.

Mr. Watts: No, sir, I don't believe that is material.

The Court: I don't think it is material unless they do give evidence one way or the other.

Mr. Watts: I think it is material that they knew it was pending. I don't want to get it in for the reason they approved of it or didn't approve of it. I think it is evidence as to the reasonableness of their vote.

The Court: Not unless you show they approved of it or that was the reason for their voting. This witness' testimony is that some of these bondholders were speculating, and they bought the bonds at $2.00 and they went up to five, [fol. 369] and they wanted to get their profit on it.

Mr. Watts: I believe it is the function of this Court at the end of this hearing to determine for itself whether or not the action of the General Mortgage bondholders in voting to reject the plan was or was not reasonably justified in the light of their relevant rights and interests and in the light of the relevant facts, and I believe for your Honor to form an informed judgment on that question it is necessary for you to know just what facts there were available for these bondholders at that time.

The Court: When these bondholders come in I will be glad to. I do not think it is material. The Court has to reach its own judgment on the financial situation and the provisions of the plan.

Mr. Watts: We conceive this to be a relevant fact, your Honor please, that the statute refers——

The Court: I have read articles in favor of the Hobbs bill, and some are much opposed to it. I hope that neither of those articles will influence me in this case.

Mr. Watts: I want to make it very clear that in offering this testimony the General Mortgage Trustee does not offer any views on the Hobbs bill.

The Court: What is the object, then?

Mr. Watts: I am sorry. I have tried to explain. It——

The Court: You want it to have some influence on the Court because you have offered it.

Mr. Watts: The only influence I want it to have on the Court, sir, is to have you consider that the General Mort-[fol. 370] gage bondholders or those of them who kept current with what was happening in the financial world and in Congress probably knew, because of the publicity given the matter in the press, that the Hobbs bill was pending at the time they were going to vote on a plan which cut them down to ten per cent of their claim and forever forfeited ninety per cent, or the rest of their claim, that there was no unanimous approval of the plan, and that the report of the Judiciary Committee on the Hobbs bill specifically referred to this Denver case as a glaring example of what was happening to junior security holders, and that the bill provided that if the bill became law, all the pending reorganization plans would become subject to it. I believe knowing that was a very material fact in considering whether it was reasonable or not for a bondholder to vote for or against the plan.

The Court: I can't agree with you.

Mr. Watts: Your Honor, I have no other questions of this witness.

Cross-examination.

By Mr. Homire:

Q. Mr. Morton, have you any information as to how many of the General Mortgage bonds now outstanding are in the hands of the same holders who held them when the reorganization proceeding commenced?

A. No, I haven't. I suppose a check of the ballots against the debtor's original list might show that, but the company itself paid interest on the bonds prior to default, and we haven't happened to do that, nor have we seen the list of the people balloting.

[fol. 371] Q. You have no record or information on that?

A. No.

The Court: Anything further of Mr. Morton?

Mr. Keegan: I don't want to ask any questions, but I have an exhibit we discussed the morning I would like to offer now.

(Thereupon a document was marked for identification City Bank Farmers Trust Company Exhibit 9-A.)

Mr. Keegan: Your Honor, we have two exhibits here marked Exhibits 9 and 9-A which we are offering as part of our evidence on the petition for adjustment as the result of the purchase of the Junction bonds. 9-A is a copy of our letter of transmittal and copies of our petition to the Commission, and Exhibit 9 is a letter from Director Sweet of the Commission to us, acknowledging receipt of the petition. In that letter——

Mr. Gibson: We are prepared to make objection to the admission of the letter, and we would prefer to do that before its contents are described by counsel.

The Court: What is the probative value?

Mr. Homire: We think it has no probative value whatever.

The Court: Just a minute. I don't know what he claims for it.

Mr. Keegan: That is what I was going to try to explain. We are contending that our petition for the construction of the plan does not involve changing the valuation or capitalization of the company in any way. It is merely an authorized adjustment within the framework of the [fol. 372] plan, and when Director Sweet acknowledged receipt of the copies of our petition he said in substance, as I remember the letter, that he had received copies of our petition for adjustment within the approved plan as the result of the purchase of the Junction bonds. We think by implication taken in connection with what we will show in our argument the Commission has been doing in other railroad reorganization cases where similar ques-

tions have come up and where they are approving this type of adjustment, that that has some significance on the way they interpret it to find what it is.

The Court: It is an action of the Interstate Commerce Commission. It is not binding upon the Commission in any way.

Mr. Keegan: No, it is not a finding in advance.

The Court: It is not even from the Commission. It is just from the director. I don't know whether this man Sweet is a member of the Commission.

Mr. Homire: He is not a member of the Commission.

The Court: Any objection to this?

Mr. Homire: We object to it.

Mr. Gibson: We object to it.

The Court: Objection sustained. Too far fetched and speculative.

Mr. Keegan: We are ready to proceed with the argument.

(Thereupon a recess of ten minutes was taken.)

Mr. Gibson: Before we proceed further, there is one point we conceive is important to have clarified. In previous hearings before your Honor on matters of general [fol. 373] concern, like the approval of the plan or the affirmance of the Salt Lake Western lease and similar matters, your Honor has made it clear from the bench that the record in all prior proceedings before this Court and the record in all prior proceedings before the Commission in this proceeding are part of the record in this hearing. We think it important that that be clarified here in the same way.

The Court: You mean that the record of the whole proceeding is considered part of this question?

Mr. Gibson: Yes, your Honor.

The Court: I think that is true, and if there is no objection it will be made part of the record.

Mr. Gibson: And could it similarly be ruled that the record at this hearing include all the certification material certified to your Honor by the Interstate Commerce Commission with respect to the balloting on the plan?

The Court: Very well. It is so ordered.

Mr. Gibson: The Clerk has physical possession of those documents here. If I could be permitted to enumerate them I think that would clarify the transcript. As I

understand it, your Honor, the certification material in the custody of the Clerk includes principally four bodies of information. One of them is a certified copy of the order of the Commission dated March 23, 1944, providing the procedure for submission to the creditors, together with exhibits attached to it. The second is a certificate of the Commission dated July 4, 1944, duly reporting to your Honor the results of the submission, and with that certificate there are submitted to your Honor (1) a list of the known holders of bonds of the several classes to whom sub-
[fol. 374] mission was made, and (2) duplicate originals of the various ballots executed by the bondholders. All of that material, we submit, should be made a part of the record at this hearing.

The Court: So ordered.

Mr. Gibson: And may we suggest to your Honor one further point, and that is that the development of the evidence this morning makes it quite clear that the issues presented by the petition of the City Bank and the issues presented by the question of confirmation of the plan, cannot feasibly be separated. Both points are urged in both the objections and the petition filed by the City Bank. We think the argument on both issues should proceed simultaneously.

The Court: Any objection to that?

Mr. Keegan: Now, if your Honor please, we would like to argue the Junction bond issue first. It is a separate question. Mr. Watts will cover our other objections.

The Court: You have two objections?

Mr. Keegan: One petition for adjustment as a result of the purchase of the Junction bonds and one objection to the confirmation of the plan.

The Court: That raises two points?

Mr. Keegan: They raise two points as far as we are concerned. I will cover the narrow issues, and Mr. Watts will cover the balance.

Mr. Homire: We didn't have an opportunity to put on one witness, Mr. Thompson.

The Court: Do you want to call him?

Mr. Homire: Just very, very briefly.

The Court: All right.

[fol. 375] Mr. Hodges: May it please the Court, while you are waiting I have received no notice of anyone's motion asking the Court to confirm this plan. I have assumed that

this hearing was called on the Court's own motion. Am I correct?

The Court: It was set for hearing on order of the Court, yes, and all parties so notified.

Mr. Hodges: I think it was set, but no party moved the Court to confirm the plan.

The Court: You mean there is no motion for the Court to act upon?

Mr. Hodges: I don't mean that, but I wanted to know whether someone had moved the Court. I don't happen to have a copy of such a motion.

The Court: I don't find a copy of such motion.

Mr. Gibson: Your Honor please, we believe that is not a necessary step in the procedure of 77. If the gentleman would be happier, we will so move now.

Mr. Hodges: Oh, that pleases me.

The Court: The order provides that the matter be set for hearing before the Court. That is notice to you all. That is due and sufficient notice to bring the matter up. All right.

Mr. Homire: Mr. Thompson said he would not be able to prepare the data until tomorrow morning.

The Court: Very well.

Mr. Keegan: These exhibits are now marked 14 to 17, and, pursuant to Mr. Gibson's request, we would like to offer those to complete the set. Mr. Gibson states I should go through these to identify them. Exhibit 14 is the income account statement for the month of October.

[fol. 376] The Court: It is not necessary. We understand what they are. Anybody that wants that information may get it.

. . . . . .

Thereupon an adjournment was taken until ten o'clock a. m. Thursday, August 31, 1944.

Pursuant to adjournment the following proceedings were had at ten o'clock a. m. Thursday, August 31, 1944:

Mr. Gibson: If your Honor please, it appears that the papers that have been certified here by the Interstate Commerce Commission as to the submission of the plan to the

creditors do not include the pamphlet that was sent around to all creditors, containing your Honor's opinion and the opinions of the Commission on the plan. We think it is appropriate to have that in the record. I have here one of the official copies.

The Court: My original opinion is in the record.

Mr. Gibson: Yes, your Honor, but this is the submission pamphlet which evidences the way the bondholders were informed. I would like to offer that in evidence.

The Court: It will be admitted.

Mr. Gibson: I suppose it will be convenient to have some way of referring to it, so I suggest Insurance Group No. 1 as the reference.

. . . . . .

[fol. 377] Mr. Watts: I would like to move this Court that the plan be not confirmed, and that it be referred back to the Commission for further consideration.

Mr. Keegan: On this question of requested adjustment within the framework of the plan as the result of the purchase of the Junction bonds, when the arguments of opposing counsel on that point are analyzed we submit that they simply go to a question as to whether the Court has the power to make that adjustment or whether it is an adjustment that the Commission only can make.

The Court: I am convinced, after reading these cases, it is only an adjustment that the Commission can make, and so it would have to go back to the Commission. I don't think I have power to change this allocation.

Mr. Keegan: Well, the Commission can't take the first step.

The Court: I don't think that was a proper procedure in the New Haven case. He said "I am going to do this, and, unless the Commission reverses me, it is going to stand," and I do not believe in that attitude. If I had felt as he did, I would have suggested I make the ruling and then let it be reversed on appeal, and not sort of dare the Commission to contradict it.

Mr. Keegan: But how is the Commission going to take the first step?

The Court: Well, I don't know. They have had this before them. They have had plenty of time to take any step they wished before they sent it to this Court.

Mr. Keegan: It has not been before the Commission since the Junction bonds were purchased.

[fol. 378] The Court: I think the Court of Appeals, if I am wrong, would tell me I should have made that change myself. I think it is really a matter for the appellate court rather than for me to do something and then tell the Commission "I have done this, and I hope you will approve of it," because the jurisdiction of the Commission and of this Court are entirely different. I do not think that both have the same jurisdiction over the same questions under these Supreme Court cases. They very clearly told this Court just what it would have to do under a reorganization plan, and what the duties of the Commission are on the application and on the capital structure. I have nothing to do with the capital structure of this reorganization plan. I simply pass it as a whole and in the view of the light of equitable principles.

Mr. Keegan: When they promulgate the plan they recognize that there are certain adjustments that have to be made.

The Court: As I tried to point out to you yesterday, I do not think this is an adjustment. It is a change in the whole capital structure that you advocate. The first mortgage bonds might come in and say "We are entitled to all these new securities because we have not been paid this bonus." I don't think it is a question to be decided by the Court. I would be very glad to consider any brief or case you want to cite before I pass on it. Does anybody want to file any memoranda or briefs on these questions?

Mr. Keegan: If you do not agree with the New Haven case there is not much point to go further with that.

The Court: I will be glad to have you file a brief on the case.

[fol. 379] Mr. Keegan: From the transcript here of the hearing in September, 1943, Mr. Homire, Colonel Anderson and Mr. Sunderland all argued that if this money was used to purchase the Junction bonds then the only way open was to make this adjustment.

The Court: Well, I can't expect counsel to be consistent in taking different cases.

Mr. Keegan: This is the same case and the same point.

Mr. Homire: That is precisely contrary to the position of that petition, as I said to Mr. Keegan.

The Court: Send the record in and make your argument on it and I will be very glad to consider it.

Mr. Honnire: We feel that the matter has been very fully presented to the Court, and it would be perfectly useless.

The Court: I will have the reporter write out the argument and I will read that, and any counsel may supplement the argument made here within ten days.

Mr. Sunderland: And reply to any brief submitted?

The Court: I don't want any brief. I will make the brief.

Mr. Sunderland: Could you make that a little longer, because we won't reach New York until Monday, and most of the time will be gone?

The Court: I will make that fifteen days. The law requires the Court to file a written memorandum, so if I have any views, that wouldn't serve any purpose today. I will keep an open mind on it until I can read these arguments and any briefs they may want to file, even though they may indicate today they are not interested in so doing.

[fol. 380] Filed United States District Court, Denver, Colorado, Jan. 10, 1945. G. Walter Bowman, Clerk.

[fol. 381]

IN UNITED STATES DISTRICT COURT

CITY BANK FARMERS TRUST COMPANY EXHIBIT 8

The Denver and Rio Grande Western Railroad Company

Interest on Unfunded Debt

	Total	Reconstruction Finance Corp.	Railroad Credit Corporation	Bank Loans	Miscellaneous	Available for Interest on Funded Debt
1943	$664,318	$574,093	$996	$76,042	$13,187	$11,116,576
1942	783,186	574,093	2,659	76,042	130,392	16,529,932
1941	1,593,645	1,372,095	2,709	76,042	142,799	2,910,045
1940	700,017	430,018	2,802	76,333	190,864	2,120,496
1939	692,938	427,674	2,794	76,042	186,428	1,213,582
1938	717,053	427,674	2,441	76,042	210,896	*493,698*
1937	612,305	427,674	4,324	76,042	104,265	*798,596*
1936	538,858	427,679	5,104	76,167	29,903	1,122,333
1935	530,388	427,077	5,921	76,250	21,140	1,929,183
1934	340,259	241,244	7,174	78,771	13,070	2,260,019
1933	258,049	157,817	13,711	83,646	2,875	3,140,746
1932	154,780	65,466	7,597	79,625	2,092	2,739,799
1931	61,838			57,854	3,984	5,142,666
1930	51,041			31,056	19,985	7,068,617
1929	27,649				27,649	8,811,533
1928	2,387				2,387	7,314,899
1927	3,604				3,604	6,472,257
1926	6,283				6,283	7,705,670
1925	18,846				18,846	6,780,296
1924	74,422				74,422	2,394,626

Italics denote debit.

[fol. 382]

IN UNITED STATES DISTRICT COURT

CITY BANK FARMERS TRUST COMPANY EXHIBIT 10

Table Showing Debtor's Income Available for Interest and Interest Requirements for All Securities Senior to General Mortgage Bonds for Each Year During Reorganization Proceedings

	I. Year	II. Debtor's Income Available for Interest	III. Debtor's Interest Requirements for Securities Senior to General Mortgage Bonds Including Interest on Unfunded Debt	IV. Surplus (or Deficit) II minus III
1.	1935 (Nov.-Dec.)	$405,418	$701,818	$-296,400
2.	1936	1,626,179	4,182,219	−2,556,040
3.	1937	−294,880	4,160,664	−4,455,544
4.	1938	10,018	4,179,725	−4,169,707
5.	1939	1,717,298	4,184,227	−2,466,929
6.	1940	2,626,847	4,206,933	−1,580,086
7.	1941	4,358,182	5,169,696	−811,514
8.	Total to 12/31/41	$10,449,062	$26,785,282	$−16,336,220
9.	Average per year to 12/31/41	$1,694,436	$4,348,556	$−2,649,120
10.	1942	$17,180,067	$4,382,701	$+12,797,366
11.	1943	11,766,711	4,368,551	+7,398,160
12.	Total for 42-3	$28,946,778	$8,751,252	$+20,195,526
13.	Average per year for 42-3	$14,473,389	$4,375,626	$+10,097,763
14.	1944	$10,277,000*	$4,357,285*	$+5,919,715*
15.	1944 (for 7 months)	5,992,635	$2,541,745	$+3,450,890
16.	Total for whole period 11/1/35 to 12/31/44	$49,672,840*	$39,893,819*	$+9,779,021*
17.	Average per year for whole period	$5,418,852*	$4,352,052*	$+1,066,800*

* Estimated as to last five months of 1944.

IN UNITED STATES DISTRICT COURT

CITY BANK FARMERS TRUST COMPANY EXHIBIT 11

Table Showing (a) Current Debtor's Income Available for Interest and (b) Surplus (or Deficit) of Total Debtor's Income Available for Interest to Last Previous December 31 *over* Interest Requirements to the Same Date of All Securities Senior to General Mortgage Bonds (Including Interest on Unfunded Debt), All as of the Respective Dates on Which the Several Plans Were Proposed—As Well as the Treatment Proposed for General Mortgage Bonds in the Several Plans.

I.	II.		III.	IV.	V.
	Date of Plan Proposal	Plan	Amount of Common Stock provided per $1000 of Gen. Mortgage claims	Current Earnings (for year in which proposal was made) per year	Accumulated Surplus (or deficit) of earnings *over* "senior" interest to last previous December 31
1.	7/28/36	Debtor's (1)	100% (Pref)	$1,626,179	$−296,400
2.	6/15/37	Insurance Group I (2)	100%	−294,880	−2,852,440
3.	8/12/38	Examiners I (3)	50%	10,018	−7,307,984
4.	7/11/39	ICC I (4)	33⅓%	1,717,298	−11,477,691
5.	4/2/40	ICC II (5)	33⅓%	2,626,847	−13,944,620
6.	1/6/41	"Discussion" (6)	50%	4,358,182	−15,524,706
7.	3/6/41	Court's (7)	32.99%	4,358,182	−15,524,706
8.	8/26/41	Examiners II (8)	33⅓%	4,358,182	−15,524,706
9.	10/8/41	Insurance Group II (9)	47.42%	4,358,182	−15,524,706
10.	7/27/42	ICC III (10)	5%	17,180,067	−16,336,220
11.	6/14/43	ICC IV (11)	10%	11,766,711	−3,538,850
12.	Date of Submission of Plans 4/28/44			10,277,000*	3,859,306
13.	Surplus of earnings over "senior interest" as of 12/31/44 (estimated as to last five months of 1944)				9,779,021*

* Estimated.

(1) Printed Record, Vol. 2, Part IV, Pages 1706–43.
(2) Printed Record, Vol. 3, Part IV, Pages 2885–2943, 2932.
(3) Printed Record, Vol. 4, Part VI, Pages 4120–4197, 4187.
(4) Printed Record, Vol. 5, Part IV, Pages 5047–5200, 5168, App. A.
(5) Printed Record, Vol. 6, Part II, Pages 5815–81, 584–1.
(6) Printed Record, Vol. 7, Part II, Pages 7352–70, 7361.
(7) Printed Record, Vol. 7, Part IV, Pages 7684–99, 7698, Ex. A.
(8) Printed Record, Vol. 8, Part I, Pages 8148–93, 8192, App. A.
(9) App. A in Ins. Group Brief dated 10/8/41 filed with I.C.C.
(10) Printed Record, Vol. 9, Part I, pages 9120–9258.

[fol. 384] IN UNITED STATES DISTRICT COURT

ORDER DENYING PETITION OF CITY BANK FARMERS TRUST COMPANY, AS TRUSTEE OF THE GENERAL MORTGAGE, FOR CONSTRUCTION OF THE PLAN AND FOR OTHER RELIEF—Filed November 25, 1944

In accordance with the Court's "Memorandum of Confirmation of Plan" heretofore filed herein, the Petition of City Bank Farmers Trust Company, as Trustee of the General Mortgage, for Construction of the Plan and for Other Relief, dated March 28, 1944, and filed herein on March 31, 1944, having heretofore been fully presented, is denied.

Dated this 29 day of November, 1944.

By the Court, J. Foster Symes, Judge.

[File endorsement omitted.]

[fol. 385]

IN UNITED STATES DISTRICT COURT

APPENDIX A TO REPORT OF INTERSTATE COMMERCE COMMISSION OF JULY 11, 1939

Finance Docket No. 11002

Denver & Rio Grande Western R. R. Co. Reorganization
Including D. & S. L. and D. & S. L. W.

	Present	Approved Plan						
	Total Debt, with interest accrued to June 30, 1938	Stock, etc.	Undisturbed or extended	First Mtge. 4% Bonds Series A	Income Mtge. 4½% bonds Series A	Preferred 5% stock Par Value $100	Common Stock No par value	
Equipment obligations	$1,795,000		$2,795,000	$	$	$	shares	
R. G. Western first trust 4s	17,316,600				(100%) 17,316,600			
R. G. Western consol. 4s	17,342,000					(100%) 17,342,000		
Junction first 5s	2,308,333				(100%) 2,308,333			
D. & R. G. consol. 4s	39,585,000				(35%) 13,854,750	(25%) 9,896,250	(40%) 158,340	
D. & R. G. consol. 4½s	7,530,760				(35%) 2,635,766	(25%) 1,882,690	(40%) 30,123	
D. & R. G. W. ref. & imp. 5s	14,250,000				(35%) 4,987,500	(25%) 3,562,500	(40%) 57,000	
D. & R. G. W. ref. & imp. 6s	2,450,000				(35%) 857,500	(25%) 612,500	(40%) 9,800	
D. & R. G. W. general mtge. 5s	37,155,800						(33⅓%) 123,786	
R. F. C. notes	11,959,469			(100%) 11,959,469				
D. & Salt Lake bonds	11,234,000			11,443,675(a)				
D. & R. G. W. trustees' certificates	5,000,000			5,000,000				
Reorganization expenses, etc.		1,000,000		1,000,000				
Chase Nat. Bank Loan	1,749,917*		1,749,917					
R. R. Credit Corp. loan, approx.	278,000		278,000					
Unsecured claims, approx.	440,000							
D. & Salt Lake minority stock		460 sh.			46,000			
D. & R. G. W. preferred stock		16,445,600						
D. & R. G. W. common stock		300,000 sh.						
Totals	171,374,879		4,822,917	29,403,144	42,006,449	33,295,940	379,049	

	Approved Plan	
	Principal Amount	Annual Charges
Equipment obligations to be assumed	$2,795,000	$98,243
Note to Chase National Bank to be extended	1,749,917*	69,997
Note to Railroad Credit Corporation to be extended if not paid in cash	278,000	4,170
New first mortgage 4 percent bonds, approx.	29,403,444	1,176,126
Total fixed interest debt	34,226,061	1,348,536
New income Mortgage 4½ percent bonds	42,006,449	
Total debt	76,232,510	
Capital Fund, maximum payment		750,000
Contingent interest		1,890,200
Sinking fund, approx.		105,046
Subtotal		4,093,842
New 5 percent preferred stock	33,295,940	1,664,797
Subtotal	109,528,450	5,758,639
New no-par common stock, shown at $100 a share	37,904,904	
Total	147,433,354	

* With interest as allowed by the court. Note to be extended at 4 percent with new collateral consisting of securities for which the present pledged securities would be exchangeable under the plan.

(a) Amount required for redemption of present bonds.

* Including $249,916.67 of interest to June 30, 1938, computed in accordance with the claim of the bank at 6 percent, from the date when the debtor filed its petition under section 77, as provided in the laws of the State of New York. The plan herein approved provides that the interest to be allowed shall be in the amount approved by the court.

[fol. 386]

IN UNITED STATES DISTRICT COURT

APPENDIX A TO REPORT OF INTERSTATE COMMERCE COMMISSION OF JULY 13, 1942

Approved Modified Plan on the Basis of Consolidation with the Denver & Salt Lake. Pledged Securities Omitted

				New Securities Assigned			
D. & R. G. W.	Claims as of Jan. 1, 1942	Undisturbed or extended	New Money	First Mtg. Bonds 3% fixed interest, 1% prior contingent interest	Income Bonds 4½% contingent interest	Preferred Stock 5%	Common Stock $100 per value
Equipment obligations	$9,139,605	$9,139,605					
R. G. West. first-trust 4's	19,443,200			71% $13,804,672	29% $5,638,528		
R. G. West. consol. 4's	19,453,200				6% 1,167,192	69% $13,422,708	25% $4,863,300
R. G. June. first 5's	2,658,333			74% 1,887,416	29% 770,917		
D. & R. G. Consol. 4's	44,362,500			23% 10,203,375	11% 4,879,875	22% 9,759,750	44% 19,519,500
D. & R. G. Consol. 4½'s	8,535,925			23% 1,963,263	11% 938,952	22% 1,877,903	44% 3,755,807
Refunding & Imp't. 5's	16,350,000			18% 2,943,000	8% 1,308,000	21% 3,433,500	53% 8,665,500
Refunding & Imp't. 6's	2,870,000			18% 516,600	8% 229,600	21% 602,700	53% 1,521,100
General mortgage 5's	42,057,755						5% 2,102,888
Chase Nat. Bank note	* 2,068,458	* 2,068,458					
R. R. Credit Corp. note	265,194	265,194					
R. F. C. notes	13,377,209			4,802,040	6,983,568	1,591,601	
Trustees' certificates	5,000,000		$**2,250,000				
Unsecured claims	* 440,000	no equity					
TOTALS, D. & R. G. W.	$186,021,379	$11,473,257	$2,250,000	$36,120,366	$21,916,632	$30,688,162	$40,428,095

Denver & Salt Lake			
Stock held by public	4,111 shares	Assigned 411,100 shares of new preferred stock	411,100
First mortgage 4's	1,500,000	1,500,000 assumed as to interest	
Income 6's	9,734,000	9,734,000 interest modified and assumed	$31,099,262

* Subject to adjustment.

** Provides for payment of $1,250,000 of trustees' certificates (balance to be paid in cash), and $1,000,000 for non-assenting D. & S. L. income bonds; approximate.

	New securities to be issued for pledge as collateral			
	First Mtge. bonds	Income bonds	Preferred stock	Common stock
Chase Nat. Bank note, extended	$1,495,044	$664,464	$1,744,218	$4,402,074
Railroad Credit Corp. note, if extended	197,938	94,666	189,332	378,664

[fol. 387]

Appendix A (Cont'd)

Capitalization and Annual Charges

	On basis of consolidation with Denver & Salt Lake		D. & R. G. W. without D. & S. L.	
	Principal	Annual charges	Principal	Annual charges
Equipment conditional sale agreements, 1941	$2,667,605	$41,979	$2,667,605	$41,979
Equipment trust I, 1941	1,260,000	30,000	1,260,000	30,000
Other equipment trusts	5,212,000	121,853	5,212,000	121,853
Total equipment obligations	$9,139,605	$193,832	$9,139,605	$193,832
Chase National Bank note	2,068,458	44,851a	2,068,458	44,851a
Railroad Credit Corp. note	265,194	2,652	265,194	2,652
R. F. C. claim (see plan)			13,377,209	535,088
Loan for new money	2,250,000	90,000	1,250,000	50,000
Denver & Salt Lake first mtg. bonds, 4% int.	1,500,000	60,000	—	—
Denver & Salt Lake income bonds, 3%–1% int.	9,734,000	292,020	—	—
	$24,957,257	$683,355	$26,100,466	$826,423
New first-mortgage bonds, 3%–1% int.	36,120,366	1,083,611	31,318,326	939,550
Total fixed interest	$61,077,623	$1,766,966	$57,418,792	$1,765,973
Capital fund, maximum payment		750,000		750,000
Prior contingent interest, 1%		473,494b		328,133bb
Sinking fund for first mtg. bonds, ½ of 1%		180,602		156,592
		$3,171,062		$3,000,698
New income bonds, 4½%	21,916,632	1,009,185d	14,933,064	694,925e
Sinking fund for income bonds, ¼ of 1%		54,792		37,333
Total debt, interest, payments to funds	$82,994,255	$4,235,039	$72,351,856	$3,732,956
New 5% preferred stock, par value $100	31,099,262	1,554,963	29,096,561	1,454,828
New common stock, par value $100	40,428,095		40,428,095	
Total capitalization	$154,521,612		$141,876,512	

Distribution of New Securities per $1000 of Present Bonds With Accrued Interest

	First mtge. bonds	Income bonds	Preferred stock	Common stock
R. G. W. firsts	$13,804,672	$5,638,528		
	908 80	371 20		
R. G. W. consols		1,167,192	$13,422,708	$4,863,300
		77 40	890 10	322 50
June. firsts	1,887,416	770,917		
	943 71	385 46		
D. & R. G. consol. 4's	10,203,375	4,879,875	9,759,750	19,519,500
	299 00	143 00	286 00	572 00
D. & R. G. consol. 4½'s	1,963,263	938,952	1,877,903	3,755,807
	307 63	147 12	294 25	588 50
R. & I. 5's	2,943,000	1,508,000	3,433,500	8,665,500
	245 25	109 00	286 13	722 12
R. & I. 6's	516,600	229,600	602,700	1,521,100
	258 30	114 80	301 35	760 55
General 5's				2,102,888
				70 55

a. Fixed interest on the $1,495,044 of new first-mtge. bonds assigned as part of the collateral for new note to Chase National Bank.

b. Comprising prior contingent interest on:

New first-mtg. bonds	$36,120,366—	$361,204
New first-mtg. bonds assigned as part of collateral for new note to Chase National Bank	1,495,044—	14,950
D. & S. L. income bonds	9,734,000—	97,340
		$473,494

bb. Comprising prior contingent interest on:

New first-mtg. bonds	$31,318,326—	$313,183
New first-mtg. bonds assigned as part of collateral for new note to Chase National Bank	1,495,044—	14,950
		$328,133

d. Comprising contingent interest on:

New income bonds	$21,916,632—	$ 986,248
New income bonds assigned as part of collateral for new note to Chase National Bank (only so much as necessary to fill out 4% interest on the note)		22,937
		$1,009,185

e. Comprising contingent interest on:

New income bonds	$14,933,064—	$ 671,988
Part of interest on new income bonds assigned to Chase National Bank note, as in d		22,937
		$694,925

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Appendix B

Approved modified Plan without consolidation with the Denver & Salt Lake. Pledged securities omitted

D. & R. G. W.	Claims as of Jan. 1, 1942	Undisturbed or extended	New Money	New Securities Assigned: First Mtg. Bonds 3% fixed interest 1% prior contingent int.	Income Bonds 4½% contingent int.	Preferred stock 5%	Common stock $100 par value
Equipment obligations	$9,139,605	$9,139,605					
R. G. West. first-trust 4's	19,443,200			71% $13,804,672	29% $5,638,528		
R. G. West. consol. 4's	19,433,200				6% 1,167,192	69% $13,422,708	25% $4,863,300
R. G. June. first 5's	2,658,333			71% 1,887,416	29% 770,917		
D. & R. G. consol. 4's	44,362,500			23% 10,203,375	11% 4,879,875	22% 9,759,750	44% 19,519,500
D. & R. G. Consol. 4½'s	8,535,925			23% 1,968,263	11% 938,952	22% 1,877,903	44% 3,755,807
Refunding and Imp't. 5's	46,350,000			18% 2,943,000	8% 1,304,000	21% 3,433,500	53% 8,665,500
Refunding and Imp't. 6's	2,870,000			18% 516,600	8% 229,600	21% 602,700	53% 1,521,100
General mortgage 5's	42,057,755						5% 2,102,888
Chase Nat. Bank note	* 2,068,458	*$2,068,458					
R. R. Credit Corp. note	* 265,194	265,194					
R. F. C. notes	*13,377,209	13,377,209	(see note)				
Trustees' certificates	5,000,000		*$1,250,000				
Unsecured claims	* 440,000	no equity					
TOTALS, D. & R. G. W.	$186,021,379	$24,850,466	$1,250,000	$31,318,326	$14,933,064	$29,099,564	$40,428,095

Denver & Salt Lake securities,
Undisturbed:
- First mortgage 4's 1,500,000
- Income 6's 9,734,000
- Stock held by public 4,111 shares

* Subject to adjustment.

Note: R. F. C. claim to be provided for by depositing the pledged securities in escrow for a specified period, the receipts from sales, dividends, and interest to be applied first to the payment of interest on the claim of $13,377,209 at 4 percent per annum, any excess to be applied to reduction of principal. For complete details, see plan.

New securities to be issued for pledge as collateral

	First Mtge. bonds	Income bonds	Preferred stock	Common stock
Chase Nat. Bank note, extended	$1,495,044	$664,464	$1,744,218	$4,402,074
Railroad Credit Corp. note, if extended	197,938	94,666	189,332	378,664

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Appendix C

On basis of consolidation with Denver & Salt Lake

		First Mtg. Bonds						Income Bonds				
	Claims as of Jan. 1, 1942	Formula Distribution	Distribution of R. F. C. excess of 2,395,841	New Allocation	Final	Formula Distribution	Deduct for foregoing increase in first mtg. bonds	New Allocation	Final	Pref. Stock	Com. Stock
R. G. Western first-trust 4's	$19,448,200	66% $12,832,512	Earnings $866,100 43.2%	$1,035,003	$13,867,515	71% $13,804,672	34% $6,610,688	$1,035,003	$5,575,685	29% $5,638,528		
R. G. Western consol. 4's	19,453,200					6% 1,167,192	—		1,167,192	6% 1,167,192	69% $13,422,708	25% $4,863,300
Junction first-trust 5's	2,658,333	66% 1,754,500	126,362 6.3%	150,938	1,905,438	71% 1,887,416	34% 903,833	150,938	752,895	29% 770,917		
D. & R. G. consol. 4's	44,362,500	21% 9,316,125		757,450	10,073,575	23% 10,203,375	13% 6,876,795	903,232	5,973,563	11% 4,879,875	22% 9,759,750	44% 19,519,500
D. & R. G. consol. 4½'s	8,535,925	21% 1,792,544	754,095 37.7%	145,782	1,938,326	23% 1,963,263				11% 938,952	22% 1,877,903	44% 3,755,807
Ref. and Imp't. 5's	16,350,000	16% 2,616,000		260,882	2,876,882	18% 2,943,000	10% 1,922,000	306,668	1,615,332	8% 1,308,000	21% 3,433,500	53% 8,665,500
Ref. and Imp't. 6's	2,870,000	16% 459,200	256,800 12.8%	45,785	504,986	18% 516,600				8% 229,600	21% 602,700	53% 1,521,100
			100.0%	$2,395,841								
General Mtg. 5's	42,057,755							$2,395,841				5% 2,102,888
R. F. C. Claim	13,377,209	7,197,881		7,197,881 4,802,040	4,802,040	36% 4,802,040	4,587,727	2,395,841		52% 6,983,568	12% 1,591,601	
				$2,395,841								
		$35,968,762			$35,968,762	$36,120,366	$22,068,235			$21,916,632	$30,688,162	$40,428,095
										D. & S. L.	411,100	
											$31,099,262	

IN THE

Supreme Court of the United States

October Term, 1945

RECONSTRUCTION FINANCE CORPORATION, INSURANCE GROUP COMMITTEE, CENTRAL HANOVER BANK AND TRUST COMPANY, TRUSTEE, UNITED STATES TRUST COMPANY OF NEW YORK, TRUSTEE, GUARANTY TRUST COMPANY OF NEW YORK, TRUSTEE, and THE CHASE NATIONAL BANK OF THE CITY OF NEW YORK, TRUSTEE,

Petitioners,

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 2906 below]

SAME

vs.

THE DENVER AND SALT LAKE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 2907 below]

SAME

vs.

CITY BANK FARMERS TRUST COMPANY, TRUSTEE, ET ALS.,

Respondents.

[Number 3106 below]

SAME

vs.

THE DENVER AND RIO GRANDE WESTERN RAILROAD COMPANY, ET ALS.,

Respondents.

[Number 3107 below]

SAME

vs.

GUY A. THOMPSON, TRUSTEE, ET ALS.,

Respondents.

[Number 3108 below]

Stipulation as to Printing of Record for Petition for Certiorari

Stipulation As To Printing of Record for Petition for Certiorari

In the first two of the above-entitled cases (Numbers 2906-2907 below, hereinafter called the Approval Appeals) the Circuit Court of Appeals for the Tenth Circuit entered an order on June 19, 1944 providing that (a) the Approval Appeals should be heard without any printed record and (b) in addition to the lengthy transcript of record certified to the Clerk of the Circuit Court by the Clerk of the District Court for the District of Colorado, there be delivered to the Circuit Court, for its use as a part of the record on the Approval Appeals, (*i*) the 10,314 pages of the printed proceedings in the District Court ("In the Matter of The Denver and Rio Grande Western Railroad Company, Debtor, In Proceedings for the Reorganization of a Railroad, No. 8669") and (*ii*) the annual reports to stockholders for the years 1936 to 1941, both inclusive, of The Denver and Rio Grande Western Railroad Company (hereinafter called the Rio Grande) and of The Denver and Salt Lake Railway Company (hereinafter called the Salt Lake). The Circuit Court entered a further order in the Approval Appeals on February 12, 1945 providing that the record therein should include the record in the last three of the above-entitled cases (Numbers 3106, 3107 and 3108 below, hereinafter called the Confirmation Appeals).

In the Confirmation Appeals an order was entered by the Circuit Court on January 17, 1945 providing that (a) the printing of the record on appeal be dispensed with and the Confirmation Appeals be heard without any printed record, (b) the record in the Confirmation Appeals should include (*i*) the record in the Approval Appeals and (*ii*) the annual reports of the Rio Grande for the years 1935, 1942 and 1943, and (c) in addition to the lengthy transcript of record certified to the Clerk of the Circuit Court by the Clerk of the

District Court, there be delivered to the Circuit Court, for its use as a part of the record on said appeals, (*i*) the "Income Account, Statement of Revenues and Expenses, Operating Performance and Statistics, Month of December, 1944," of the Rio Grande, (*ii*) the "Income Account and Financial Exhibit for the Period Ended December 31, 1944" of the Rio Grande, (*iii*) the annual report to stockholders for the year 1943 of the Salt Lake and (*iv*) the "Income, Profit and Loss and General Balance Sheet, December 31, 1944" of the Salt Lake.

All said appeals were heard in the Circuit Court without any printed record except for the documents, referred to above, that were already otherwise available in printed form. A decree was entered by the Circuit Court in all said appeals on May 10, 1945.

The parties hereinabove named as Petitioners are filing a petition (hereinafter called the Petition) for writs of certiorari to the Circuit Court to review that decree.

The persons whose names are signed hereto by counsel (hereinafter sometimes called the undersigned) are all the persons interested in the Petition. The undersigned are hereinafter sometimes referred to as (*i*) the Interests of Group 1, being the six parties hereinabove named as Petitioners; (*ii*) the Interests of Group 2, being all the appellants in the Circuit Court, namely, The Denver and Rio Grande Western Railroad Company (appellant in No. 2906 below and in No. 3107 below), The Denver and Salt Lake Western Railroad Company (appellant in No. 2907 below and in No. 3107 below), City Bank Farmers Trust Company as Trustee (appellant in No. 3106 below) and Guy A. Thompson, Trustee (appellant in No. 3108 below); (*iii*) Interests of Group 3, being all the other persons in behalf of whom appearances were entered in the Circuit Court (though none of the Interests of Group 3 otherwise participated in the

proceedings in the Circuit Court); and (*iv*) Interests of Group 4, being all the other persons* named as appellees in the notices of appeal filed in the District Court in any of said appeals, or in the titles of any of said appeals in the Circuit Court (though none of the Interests of Group 4 appeared or participated in the Circuit Court). None of the other persons who participated before the District Court or the Commission was named as an appellee, or appeared, or participated in the proceedings in the Circuit Court.

All of said material constituting the record in all of said appeals in the Circuit Court has, together with a transcript of the proceedings in the Circuit Court, been delivered to the Clerk of the Supreme Court. The undersigned desire to stipulate in accordance with paragraph 8 of Rule 38 of the Supreme Court to omit from the printed record all matter not essential to a consideration of the questions presented by the Petition.

NOW, THEREFORE, subject to the approval of the Supreme Court, the undersigned hereby stipulate and agree that:

1. For the purpose of the Petition, but not of any subsequent proceedings in the Supreme Court if the Petition be granted, the printed record shall consist of the following and only the following:

(a) The pamphlet entitled "Submission of Plan of Reorganization Pursuant to Section 77 of the Bankruptcy Act, as Amended," introduced at the hearing before the District Court on August 30, 1944 (Circuit

*Except "The First National Bank of New York" which was, by error, named as appellee in the notice of appeal by Guy A. Thompson, Trustee.

Court's Transcript in the Confirmation Appeals, p. 93, D. Ct. Transcript p. 119).

(b) "Memorandum" of the District Court dated November 1, 1944, confirming the Plan (Circuit Court's Transcript in the Confirmation Appeals, beginning at p. 433 of volume II).

(c) Order of the District Court dated November 29, 1944, confirming the Plan (Circuit Court's Transcript in the Confirmation Appeals, beginning at p. 473 of volume II).

(d) Opinion and concurring opinion in the Circuit Court dated May 10, 1945, disapproving the orders of the District Court (Transcript of Proceedings in the Circuit Court at pp. 601-626).

(e) Order of the Circuit Court dated May 10, 1945 reversing the orders of the District Court (Transcript of Proceedings in the Circuit Court at p. 627).

(f) The oral opinion of the District Court delivered on September 14, 1943 appearing at pages 144-146 of volume I of the transcript before the Circuit Court in the Confirmation Appeals (pages 181-183 of the District Court transcript).

(g) Order number 484 of the District Court beginning at page 1828 of volume 3 of the transcript before the Circuit Court in the Approval Appeals.

(h) Certificate of Interstate Commerce Commission dated July 4, 1944 concerning results of submission of Plan to creditors, beginning at page 158 of volume I of the transcript before the Circuit Court in the Confirmation Appeals.

(i) That portion of the transcript of the hearing before the District Court on August 30-31, 1944 beginning with the word "In" in line 1 of page 1 of the copy before the Circuit Court in the Confirmation Appeals and continuing through the word "doing." on page 96, being all of the Circuit Court record of the testimony at such hearing, appearing at pages 192-288 of volume II of the transcript before the Circuit Court in the Confirmation Appeals.

(j) The following exhibits (or portion thereof) introduced at the hearing referred to in (i) above and appearing at the following pages of volume II of the transcript before the Circuit Court in the Confirmation Appeals: (*i*) only the first table (entitled "Interest on Unfunded Debt") on page 32 of the 1943 Annual Report introduced as City Bank Farmers Trust Company Ex. 8 beginning at page 353 and appearing at page 385; (*ii*) City Bank Farmers Trust Company Ex. 10 appearing at page 396; and (*iii*) City Bank Farmers Trust Company Ex. 11 appearing at page 397;

(k) The order of the District Court entered on November 29, 1944 denying the petition of City Bank Farmers Trust Company, Trustee, appearing at page 483 of volume II of the transcript before the Circuit Court in the Confirmation Appeals.

(l) The following tables attached as exhibits to the reports of the Interstate Commerce Commission and appearing at the following pages of volume 2 of the transcript before the Circuit Court in the Approval Appeals: (*i*) Exhibit A to the report of July 11, 1939 appearing between pages 1308 and 1309 (printed proceedings in the District Court, between pages 5168 and 5169); and (*ii*) Appendices A, B and C to the report of

July 13, 1942 appearing on pages 1667-1670 (printed proceedings in the District Court pages 9203-6).

(m) This Stipulation.

2. For the purposes of the printed record referred to in 1. above, the pamphlet referred to in 1.(a) and this Stipulation need not be reprinted but for the convenience of the Supreme Court Petitioners may deliver to the Clerk 40 or more copies thereof in their original ptinted form, to be bound with the other papers designated in 1. above when printed.

3. All the undersigned reserve the right to refer to any portion of the record certified from the Circuit Court to the Clerk of the Supreme Court.

4. In the event that the Petition be granted, the printed record for further proceedings thereon in the Supreme Court shall consist of (*i*) the printed record referred to in 1. above (as Volume I), and (*ii*) such portions of the entire record certified by the Circuit Court to the Clerk of the Supreme Court as the respective Interests of Groups 1 and 2 may designate for such purpose.

5. For the purpose of any other petition or petitions for certiorari that may be filed by any of the undersigned, but not of any subsequent proceedings in the Supreme Court in relation to any such other petition if granted, the printed record shall be the printed record prepared pursuant to 1. above and such printed record may be used by, and shall be deemed to have been filed by, any of the undersigned filing such other petition. In the event that any such other petition be granted, the printed record for further proceedings thereon in the Supreme Court shall consist of (*i*) the printed record prepared pursuant to 1. above (as Volume

I), and (*ii*) such portions of the entire record certified by the Circuit Court to the Clerk of the Supreme Court as the respective Interests of Groups 1 and 2 may designate for such purpose.

6. Service of the printed record, the Petition and any other petition for certiorari that may be filed, all briefs and all notices, both in connection with the Petition and any such other petition and in connection with subsequent proceedings in the Supreme Court if the Petition or any such other petition be granted, is hereby waived with respect to all Interests of Groups 3 and 4 except that one copy of each such paper shall be served on counsel for the Debtor Trustees of the Rio Grande.

7. This Stipulation may be executed in any number of counterparts, all of which together shall constitute but one instrument. The signatures hereto need not be on the same counterpart, but each signature, or any number of signatures, may be on different counterparts, or may be on separate signature sheets to be annexed to the text hereof. Execution hereof by the Interests of Groups 3 and 4 shall not impair the liberty of any of said persons, or of any other persons, to claim that they are, or are not, parties to the proceedings in the Supreme Court.

Dated as of July 16, 1945.

Interests of Group 1

Signatures of Counsel	Addresses
Hugh B. Cox HUGH B. COX *Acting Solicitor General of the United States*	Washington, D. C.
and	
W. Meade Fletcher, Jr. W. MEADE FLETCHER, JR. *Chief Railroad Counsel, Reconstruction Finance Corporation* *For Reconstruction Finance Corporation*	811 Vermont Ave., N. W. Washington 25, D. C.
Henry W. Anderson HENRY W. ANDERSON	Electric Building Richmond 12, Va.
and	
George D. Gibson GEORGE D. GIBSON. *For Insurance Group Committee*	Electric Building Richmond 12, Va.
Alexander M. Lewis ALEXANDER M. LEWIS *For Central Hanover Bank and Trust Company, Trustee*	70 Broadway New York 4, N. Y.
Edwin S. S. Sunderland EDWIN S. S. SUNDERLAND	15 Broad Street New York 5, N. Y.
and	

James L. Homire — 15 Broad Street, New York 5, N. Y.

JAMES L. HOMIRE
For Guaranty Trust Company of New York, Trustee

W. A. W. Stewart — 45 Wall Street, New York 5, N.Y.

W. A. W. STEWART
For United States Trust Company of New York, Trustee

Arthur A. Gammell — 15 Broad Street, New York 5, N.Y.

ARTHUR A. GAMMELL
For The Chase National Bank of the City of New York, Trustee

Interests of Group 2

William V. Hodges — Equitable Building, Denver 2, Colorado

WILLIAM V. HODGES

and

F. C. Nicodemus — 40 Wall Street, New York 5, N. Y.

F. C. NICODEMUS
For (i) The Denver and Rio Grande Western Railroad Company, and
(ii) The Denver and Salt Lake Western Railroad Company

Edward E. Watts, Jr.	20 Exchange Place New York 5, N. Y.
EDWARD E. WATTS, JR.	
and	
Milton J. Keegan	First National Bank Denver 2, Colorado
MILTON J. KEEGAN *For City Bank Farmers Trust Company, Trustee*	
H. H. Larimore	Missouri Pacific Bldg. St. Louis 3, Missouri
H. H. LARIMORE *For Guy A. Thompson, Trustee of Missouri Pacific Railroad Company*	

Interests of Group 3

Henry McAllister	Equitable Building Denver 2, Colorado
HENRY McALLISTER *For Wilson McCarthy and Henry Swan, as Trustees of The Denver and Rio Grande Western Railroad Company*	
Erskine R. Myer	Midland Savings Bldg. Denver 2, Colorado
ERSKINE R. MYER *For (i) H. Allyn Hicks, Jr., Trustee of The Denver and Salt Lake Western Railroad Company;* *(ii) Moffat Tunnel Improvement District, and* *(iii) Moffat Tunnel Commission*	
Paul D. Miller	20 Pine Street New York 5, N. Y.
PAUL D. MILLER *For The Chase National Bank of the City of New York*	

Interests of Group 4

H. Lawrence Hinkley	State Capitol Bldg. Denver, Colorado
H. LAWRENCE HINKLEY *Attorney General* *For (i) State of Colorado; and* *(ii) Public Utilities Commission of Colorado*	
Jesse E. Waid	14 Wall Street New York 5, N. Y.
JESSE E. WAID *For Bankers Trust Company, Trustee*	
S. Arthur Henry	Colorado Nat'l. Bank Bldg. Denver 2, Colorado
S. ARTHUR HENRY *For General Securities Company*	
Harry Hoffman	30 Pine Street New York 5, N. Y.
HARRY HOFFMAN *For Untermyer Family Group*	